

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

COMMONWEALTH EDISON COMPANY	:	
	:	
Petition for approval of delivery services tariffs and	:	
tariff revisions and of residential delivery services	:	No. 01-0423
implementation plan, and for approval of certain	:	
other amendments and additions to its rates, terms,	:	
and conditions.	:	

**REPLY BRIEF OF
COMMONWEALTH EDISON COMPANY**

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REPLY BRIEF OF COMMONWEALTH EDISON COMPANY

INTRODUCTION

In August 1999, in the wake of severe outages in downtown Chicago, ComEd assured the public that it would undertake a comprehensive effort to identify and repair the problems. ComEd has delivered on those assurances. It restored service, investigated the causes of the outages, and inspected the transmission and distribution systems. It also developed and executed a prudent plan -- without excess cost -- to install facilities and procedures to provide reliable service. As a result of ComEd's investigation and subsequent capital investments and operating improvements, customers today are receiving significantly better service than they were in 1999.

ComEd also committed in August 1999 that customers would not bear the costs of the investigation that ComEd was undertaking. ComEd performed the investigation on an expedited basis. The costs of those activities were incurred largely in 1999 and were not passed on to customers because ComEd's bundled rates were -- and are -- frozen. In fact, under the law, customers received an additional 5% rate cut, reducing rates below the levels being paid in 1999.

In preparing its rate filing, ComEd engaged in an exhaustive analysis of all costs incurred, disaggregated the components of each major capital expenditure, and ensured that its proposals did not include imprudent or unnecessary costs or non-recurring expenses. ComEd did not simply assert that such costs were excluded, but painstakingly assembled the detailed back-

up data demonstrating that no imprudent or unnecessary costs were included in its proposed revenue requirement.

Staff, however, speculates that “[i]f ComEd had been adequately maintaining and upgrading their distribution system all along, the work ComEd crammed in a few short months could have been done in a controlled manner, over a longer period of time, and at a lower cost.” Staff Brief (“Br.”) at 32. GC and the ARES Coalition similarly question whether ComEd’s efforts to fix the problems that arose during the Summer of 1999 “resulted in any additional costs in [ComEd’s] proposed revenue requirement.” GC Br. at 23. And months after ComEd filed the rate case, GC, the ARES Coalition and Staff have requested an audit “for the purpose of sorting out those costs that Edison incurred as a result of well documented maintenance and past mismanagement of its distribution system.” ARES Br. at 12. These parties, though, have simply failed to analyze the evidence and ComEd’s extensive responses to discovery in this case.

Whatever additional expenses were incurred for the 1999 investigative effort have been excluded from ComEd’s delivery services revenue requirement in this case as well. They are necessarily excluded because the revenue requirement is based on a 2000 test year, which does not include the 1999 expenses. In one area where the investigative costs spilled over into 2000 -- the Liberty and Vantage reports -- ComEd deducted the costs from test year 2000 expenses.

ComEd did not, however, simply investigate the problem and perform short-term repairs. It also made the necessary capital investments to add capacity to meet load growth and to improve reliability. Significantly, ComEd made those investments pursuant to a prudent plan, without excess costs, through increased efficiency and productivity. Helwig, Tr. 2716:6-2717:7. And ComEd ensured that no excessive or unnecessary capital costs had been incurred and reflected in its rate proposal, by disaggregating and separately evaluating each component of the

major capital distribution projects. DeCampli, Tr. 1439:22-1440:11. For example, analysts disaggregated the transformer and other major components of the projects to determine whether the prices paid were reasonable and in line with industry norms for comparable work. The analysis revealed that the prices ComEd paid, including the time-based incentives, overtime, and other contract terms questioned by Staff and GC, were consistent with prevailing costs. DeCampli, Tr. 1439:22-1440:11; Williams, Tr. 859:17-861:10; Voltz Reb., ComEd Ex. 24.0 CR, pp. 7:129-9:175. Additional examples of the process ComEd followed and the analyses ComEd performed to assure that there were no inflated costs in its proposed rate base are described in Sections II.C.6. and II.D.4 below.

ComEd also presented evidence on the issue that GC, Staff and the ARES Coalition have raised about basing rates on a 2000 test year – whether the expenses incurred during that year are typical or whether they include excessive or nonrecurring items for which adjustments should be made. The choice of the year, of course, was essentially preordained. The Commission has discouraged use of future test years for ratemaking purposes, effectively foreclosing that option. And a 2000 test year was the only realistic alternative because it is the most recent year for which the relevant information is available.

More importantly, the 2000 test year costs are reasonable. They are not affected by the investigative costs incurred in 1999. In addition, ComEd reviewed the test year 2000 costs for any inappropriate amounts. For example, ComEd removed all costs related to implementing the Unicom/PECO merger, the nonrecurring portion of obsolete material write-offs during the year, the costs of the discontinued Light Bulb Program, and reserved but not yet incurred environmental remediation expenditures. Hill Dir., ComEd Ex. 4.0 CR pp. 26:546-28:599.; Voltz Sup. Reb., ComEd Ex. 39.0, p. 3:45-57. ComEd also reduced storm restoration costs from

the actual year 2000 level by \$3 million by averaging the costs incurred in 1998, 1999 and 2000 to arrive at a better indication of ongoing storm damage cost. In addition, ComEd compared 2000 test year costs to actual expenses incurred and projected for 2001 and found that 2000 cost levels are not atypical and, if anything, understate the actual costs that ComEd is incurring in 2001. Helwig Sur., ComEd Ex. 43.0, p. 3:65-68; Voltz Dir., ComEd Ex. 5.0, pp. 19:403-23:485. Thus, the 2000 test year expense levels, though higher than expense levels in 1997, the test year in ComEd's last delivery services rate case, are representative of the ongoing costs of providing significantly more reliable service to a growing customer load.

Contrary to the suggestion of some intervenors, ComEd did not merely assert that its methodology was correct and ask the Commission to trust ComEd's conclusions. It produced the data underlying and supporting the analysis, including a vast volume of data concerning its books and records, costs, assets, revenues, customers' usage and costs, employee compensation, and overhead. It included tens of thousands of pages of data relating to the planning and project management of virtually every recent material project or system program. Juracek Sur., ComEd Ex. 41.0, pp. 8:206-9:255.

The result of this thorough process cannot be overstated. With the exception of several issues raised by Staff witness Bruce Larson and answered in detail by ComEd, not one instance of any enhanced, inflated or escalated costs has been identified by any party for any plant, substation or other facility. Effron, Tr. 2106:2-15; Schlissel, Tr. 2209:6-12. Not one.

Frustrated by the lack of evidence that significant costs should be disallowed, some parties have decided, late in the case, to ask that the Commission simply set aside the massive evidentiary record developed in this docket, suspend the proceeding, and mandate the performance of an independent audit. It is not ComEd's practice to comment on other parties'

case management, but intervenors in this case have put it in issue. The schedule in this case allotted three months for intervenors to prepare their analyses. (Indeed, all knew when this case would be filed, and in view of that, advance planning, such as retention of experts, might have been prudent.) Nonetheless, some of the intervenors who now claim that an independent audit is necessary did not even hire experts until two months after the case was filed. The vast majority of the material ComEd made available was not even reviewed by the intervenors' experts. Intervenors' failure to make more than a cursory review of the detailed data ComEd provided does not equate to a failure of proof on ComEd's part, and certainly provides no basis for scrapping this case and ordering an audit.

In short, the real claim that ComEd confronts in this proceeding is not that it has failed to prove its case, but that it has not disproven the speculation by commenters who failed to analyze fully the evidentiary record, the materials made available in discovery, and the other publicly available data. ComEd looked for excessive costs and excluded them. It made the supporting materials available, and no party can point to any evidence of inflated costs of the type that they now speculate may theoretically exist.

The Commission has all the information it needs to reach a final decision in this case establishing delivery services rates for all customers in the new unbundled, competitive market. ComEd has shown that its capital investments are prudent and reasonable, and is entitled to have these investments included in its rate base. The suggestion that ComEd's August 1999 assurances stated or implied that capital investments that are needed to serve new load and to provide reliable service for decades into the future would never be included in ComEd's rate base is plainly wrong. Those investments would have been made regardless of the 1999 outages

and the costs ComEd incurred were no higher than the costs that any comparable utility would have incurred to do the same work.

It is important to recognize that a significant portion of the increase in the revenue requirement has nothing to do with any of the questions underlying the request for an audit, relating instead to (1) costs that the Illinois Appellate Court recently ruled were improperly excluded from ComEd's initial delivery service rates, (2) delivery costs that were previously allocated to the generation function that ComEd no longer owns or operates, and (3) normal inflation and the like. In addition, ComEd has already agreed to reduce its proposed revenue requirement increase by nearly 20% -- over \$100 million -- reflecting ComEd's willingness to consider Staff's positions and compromise when issues are debatable. Hill Sur. ComEd Ex. 45.0 p. 38:813-17; Staff Br. at 95-97. But there is no room for debate about the remaining core expenses necessary to provide reliable delivery services. The undisputed evidence that ComEd's proposed rates are significantly below the delivery services rates of many other peer group utilities simply confirms that ComEd's costs are not inflated. Juracek Dir., ComEd. Ex. 1.0, 20:506-18.

For these reasons, the Commission should approve ComEd's new delivery services rates on the existing record, without any further audit or inquiry.

ARGUMENT

I.

Legal Issues and Standards for Decision

A. Substantive Standards and Policies Governing Requested Rates

ComEd's Initial Brief (at 25-28) addresses most issues raised by others. Staff stresses that Section 16-108 of the Public Utilities Act (the "Act"), 220 ILCS 5/16-108(c), does not

mandate “full” cost recovery when it directs that delivery services rates be “cost based” and “shall allow the electric utility to recover the costs of providing delivery services....” Given that the rates “shall” allow ComEd to recover its costs, the absence of “full” is of no significance. The Commission also recently confirmed that “utilities are indeed entitled to the opportunity to obtain full recovery of their revenue requirements....”, *Commonwealth Edison Co. v. Illinois Commerce Comm’n*, Nos. 2-00-0275 and 2-00-0375 (consol.) (Ill. App. Ct.), ICC Br. at 17. In any event, Staff’s discussion is irrelevant because its only conclusion from the absence of “full” concerns out-of-period expenses (Staff Br. at 3-4) on which ComEd’s rates are not based.

BOMA contends that, under Section 9-241, delivery customers must be treated in “the same manner as bundled service customers in terms of rate design.” BOMA Br. at 4. TrizecHahn claims that Section 16-108(c) requires delivery services rates to be “nondiscriminatory.” TrizecHahn Br. at 6-9. Neither claim has merit. Section 9-241 does not prohibit differences between bundled and delivery services rates and rate design, and Section 16-111(a) freezes bundled rates “notwithstanding any provision of Article IX.” Section 16-108(c) concerns delivery services rates only, not their differences from bundled rates. TrizecHahn’s position is also inconsistent with its efforts to maintain significant cross subsidization under Rider HVDS. *See* Section II.G.2. TrizecHahn’s argument that any rate increase should be allocated “across the board” is discussed in Section II.F.2.

The ARES Coalition’s argument that Section 16-111(a) freezes delivery services rates (ARES Br. at 21-34) has already been considered and properly rejected in connection with the denial both of the “Joint Motion to Strike” and its petition for interlocutory review thereof. ComEd incorporates herein its responses to those pleadings. *See also* ComEd Br. at 8-9.

B. Procedural Issues (e.g., Admissibility) Not Addressed in Specific Arguments

GC repeats its request that the Commission depart from Illinois law and establish its own special standards for affording confidential treatment to documents. GC errs, as shown in ComEd's response to the City's petition for interlocutory review, incorporated herein.

C. Other Policy Issues

1. Impact on Customers

Contrary to the evidence, the ARES Coalition claims that ComEd did not assess the impact of its proposal on customers, who they say will pay more because CTCs will not offset the increase in ComEd's revenue requirement. ARES Br. at 46-53. ComEd clearly did assess the impact of its proposal, and presented studies showing that well over 90% of ComEd's non-residential customers are in customer classes or groups that will have positive CTCs even under ComEd's proposal. ComEd Br. at 31-33. For these classes and groups, the CTC fully offsets any change. Similarly, the ARES Coalition's contention that ComEd's proposed transmission rates will have significant customer impacts (ARES Br. at 48-49) is untrue. FERC terminated ComEd's transmission rate case on December 20, 2001. *Alliance Companies, et al.*, 97 FERC para. 61,327 (December 20, 2001). In any event, its impact would have been very limited. ComEd Br. at 32. The ARES Coalition's contrary claims are based on CTC calculations that use unrealistic market values. ComEd Br. at 32-33.

BOMA's and TrizecHahn's contention that differences between frozen bundled rates and cost-based delivery services rates cause impermissible customer impacts (BOMA Br. at 47; TrizecHahn Br. at 9-12) is also incorrect. ComEd Br. at 33-34, 137-38; Section I.A, *supra*.

NEMA contends (NEMA Br. at 4-5) that marginal cost-based delivery services rates will make it more difficult for customers to see prices for specific services that NEMA says are

“hidden in their bundled service rates” and will hurt those who relied on “Commission precedent.” NEMA overlooks that, for nearly two decades, the Commission employed marginal cost ratemaking for ComEd’s bundled rates. NEMA also ignores the overwhelming evidence that marginal cost-based rates promote economic efficiency, reduce subsidies, and send economically correct price signals. ComEd Br. at 103-08; Section II.F., *infra*.

2. Impact on Cost Based Rates

The ARES Coalition’s challenges to ComEd’s direct assignments and allocations must be rejected for the reasons stated in Sections II.C.1 and II.D.3.a.

3. Impact on the Development of an Effectively Competitive and Efficient Electricity Market

The claims of BOMA, TrizecHahn, and the ARES Coalition about the supposed impact of ComEd’s proposal on the development of a competitive market should be rejected. ComEd’s proposal will promote efficiency and support the reliable delivery system required for competition. Juracek Reb., ComEd Ex. 20.0, p. 6:164-69; Strobel Reb., ComEd Ex. 18.0, pp. 2:27-4:75. Arguments concerning the effect of rate increases on customers’ incentives to switch are addressed in Section I.C.1., II.G.1.c and II.G.10 herein and at ComEd Br. at 31-34, 136-138. TrizecHahn’s argument about Rider HVDS is answered in Section II.G.2; BOMA’s contention concerning differences between bundled and delivery services rate design in Section II.G.2.e and ComEd Br. at 33-35; and the ARES Coalition’s claim that the Commission must protect RESs’ profit margins by setting below-cost delivery services rates in ComEd Br. at 3-4.

4. Impact on Future Rate Cases

The ARES Coalition’s claims about the impacts of this case on future rate cases were answered on pages 39-41 of ComEd’s Initial Brief. ComEd has proven its case and should be allowed the opportunity to recover its costs attributable to load growth and reliability.

5. Impact on Capital Markets and Cost of Capital

See Section II.E, *infra*.

6. Impact on Distribution Adequacy and Reliability

The ARES Coalition wants to summarily dismiss ComEd request to increase non-residential rates, attributing any cost increase to past failures. ARES Br. at 56-57. The evidence demonstrates that this is not so. *See* Introduction and Sections II.C.6, II.D.4. BOMA acknowledges the evidence that the revenue requirement includes only the reasonable costs of a reliable distribution system, but complains that many of its members are also required by the City of Chicago to install emergency generators. BOMA Br. at 8-9. Although BOMA recognizes that the Commission cannot relieve its members of this obligation, it stresses that rates should include only the costs of a reliable system. That is exactly what ComEd proposes in this case; there are no inflated costs of the type that BOMA seeks to avoid.

II.

Revenue Requirement Issues

A. Calculation of Revenue Requirement

ComEd's revised proposed jurisdictional revenue requirement, reflecting the reduced rate of return and the downward adjustments to net rate base and operating expenses made or agreed to in ComEd's rebuttal and surrebuttal testimony, is \$1,682,705,000, a decrease of \$104,265,000. ComEd Br. at 41 & App. A. ComEd's proposal is only 10.7% larger than Staff's revised proposed revenue requirement of \$1,520,355,000. Staff Br. at 6.

The ARES Coalition's and GC's continued references to a "47.5%," "47%," or "almost 50%" increase from the revenue requirement approved in Docket No. 99-0117, and to a "36.7%" increase in the resulting charges (*e.g.*, ARES Br. at 3; GC Br. at 19-30) are inaccurate and misleading. ComEd's revised proposed revenue requirement is approximately 38.9% higher

than the \$1,211,470,000 approved in Docket No. 99-0117 and only 17.9% higher than requested there. *Commonwealth Edison Co.*, Docket No. 99-0117 (Rehearing Order, March 9, 2000), App. A, Sch. 1. ComEd's revised proposal increases overall jurisdictional charges only approximately 28.7% (ComEd Br. at 37) because, from 1997 to 2000, ComEd experienced an approximately 7.9% increase in billing determinants. Juracek Dir., ComEd Ex. 1.0, p. 20:506-18; Effron Reb., GC Ex. 5.0, p. 5:10-13. In addition, the "increases" are in large part nominal rather than real:

- There was inflation from 1997 to 2000. Taking into account an annual inflation factor of 3.5%, which Staff used in calculating adjustments, is appropriate. *E.g.*, Sant Sup. Dir., Staff Ex. 14.0, Sch. 14.7, line 10; Voltz Sup. Reb., ComEd Ex. 39.0, p. 2:33-44. Over 3 years, this would compound to nearly 10.9%.
- ComEd had substantial growth in load and billing determinants. ComEd's net weather-adjusted system load increased by 10.0% (Staff Cross Ex. 18), and its billing determinants increased by approximately 7.9%. Juracek Dir., ComEd Ex. 1.0, p. 20:506-18; Effron Reb., GC Ex. 5.0, p. 5:10-13.
- ComEd refunctionalized additional plant to distribution. The revenue requirement includes \$27 million of operating expenses properly refunctionalized under FERC's "seven factor" test that were not reflected in Docket No. 99-0117. *E.g.*, Born Dir., ComEd Ex. 17.0, p. 6:120-33; Voltz Reb. ComEd Ex. 24.0 CR, p. 11:212-15. That refunctionalization is "zero sum" between Illinois rates and FERC transmission rates, i.e., there is no double counting. ComEd Br. at 3, 42-43.
- A substantial portion of the apparent "increase" is due to other appropriate accounting changes, including changes ordered by the Commission in Docket No. 99-0117. *E.g.*, Voltz Reb., ComEd Ex. 24.0, CR, p. 11:210-12; Hill. Sup. Reb., ComEd Ex. 38.0, pp. 7:150 - 8:162; Hill Sur., ComEd Ex. 45.0, pp. 2:42 - 3:48, 5:88 - 6:118, 10:217-28. The largest related to booking distribution-related incentive compensation to distribution accounts, which made a \$39.5 million difference "on paper" from 1999 to 2000. *E.g.*, Voltz Reb., ComEd Ex. 24.0, CR pp. 11:210-12.
- A substantial portion of the apparent "increase" is due to cost disallowances of approximately \$23 million in Docket No. 99-0117 that were reversed on appeal, and now are before the Commission on remand.
- A substantial portion of the apparent "increase" is due to the far more accurate combination of assignment and allocation of General and Intangible Plant, and A&G expenses used in this Docket, discussed in detail in Sections II.C.2 and II.D.3.b, *infra*. ComEd's proposal uses a more accurate assignment and allocation process reflecting ComEd's restructuring into a "wires company", the transfer of its fossil and nuclear generation, and the transfer of other functions to separate Exelon business units. The difference, as measured against the use of

an inaccurate general labor allocator, is \$404,605,000 in General and Intangible Plant (rate base) and \$36,240,000 in A&G expenses.

All of those points are apart from the fact that over 90% of ComEd's non-residential customers are in classes or groups with positive CTCs, which offset any real increase in jurisdictional delivery service charges, effectively funding the remaining increase through reductions in ComEd's stranded cost recovery. *E.g.*, ComEd Br., at. 22-24. Finally, GC's "prudence" arguments (GC Br. at 19-25) are unsupported and incorrect. *See* Section II.C.6.

B. Selection of Test Year

2000 is indisputably the most appropriate test year for this proceeding. *See* ComEd Br. at 41-42. Several parties argue for an "audit" or for disallowances, claiming that 2000 was or might have been an atypical year. Staff Br. at 6; ARES Br. at 61-64; BOMA Br. at 9-10; GC Br. at 25-26. None of these arguments is correct (*see* Section II.C.6) and, in any event, no one has proposed a different test year. Their arguments also fail by focusing largely on the distribution capital additions portion of the rate base which is evaluated on a cumulative, rather than on a test year, basis. ComEd Br. at 10 n.1, 13, 51.

C. Rate Base

ComEd's revised proposed net rate base is \$4,018,471,000. ComEd Br. at 42. Setting aside Staff's erroneous proposed adjustment based on the less accurate general labor allocator for all General and Intangible Plant (*see* Section II.C.2), ComEd's revised proposal is 0.754% lower than Staff's revised proposed net rate base of \$4,048,773,000. Staff Br., App. A, Schs. 3, 4.

ComEd's revised proposed jurisdictional Distribution Plant (which includes distribution-related customer plant), net of accumulated depreciation, is \$4,548,019,000. ComEd Br., App. A, Sch. B-1. That figure is only 0.765% higher than Staff's corresponding figure of \$4,513,477,000. Staff Br., App. A, Sch. 3. ComEd's and Staff's figures for gross General and

Intangible Plant and the associated accumulated depreciation differ only because of Staff's use of a general labor allocator. ComEd's net figure for the remaining components of its proposed net rate base, negative \$1,155,692,000, is 5.998% lower than Staff's corresponding figure. ComEd Br., App. A, Sch. B-1; Staff Br., App. A, Sch. 3.

1. Functionalization of Distribution Plant

ComEd correctly functionalized distribution plant. ComEd Br. at 42-45. The evidence is uncontradicted. None of the ARES Coalition's specious claims regarding supposed allocations to the distribution function of "supply" (generation) costs relates to distribution plant. ARES Br. at 13, 56, 59, 65, 69-70, 79, 90, 98, 117.

**2. General and Intangible Plant --
Direct Assignment and Allocation**

ComEd is now a different company from the one in Docket No. 99-0117, although Staff and certain intervenors want to pretend otherwise.

- Docket No. 99-0117 involved a 1997 test year. *Commonwealth Edison Co.*, Docket No. 99-0117 (August 26, 1999), p. 9. ComEd in 1997 was a vertically integrated electric utility. It owned numerous fossil generating plants and the nation's largest nuclear fleet.
- This case uses a 2000 test year, with appropriate adjustments. *See* Section II.B. By December 1999, ComEd had sold all its fossil units. By January 2001, ComEd formally was restructured into separate entities. Generation and other competitive businesses were separated from the "wires company" and given separate balance sheets that accurately assigned assets and liabilities. *E.g.*, Hill Dir., ComEd Ex. 4.0 CR, pp. 8:168-9:174; Strobel Reb., ComEd Ex. 18.0, pp. 6:130-7:138; Hill Sur., ComEd Ex. 45.0, pp. 5:104-6:110. The movement of entities, departments, and personnel and the accounting necessary to implement the restructuring occurred during the test year, beginning in August or September 2000. *E.g.*, Hill Reb., ComEd Ex. 23.0 CR, pp. 6:114-16, 7:149-53, ComEd Ex. 23.1; Hill, Tr. 3203:10-3206:5, 3210:3-18, 3211:6-11, 3545:9-3546:13.
- ComEd's independent auditor, Pricewaterhouse Coopers ("PWC"), reviewed the balance sheets of the restructured entities and, in large part, their other financial statements, and found no irregularity. *E.g.*, Hill Dir., ComEd Ex. 4.0 CR, p. 9:175-76; Strobel Reb., ComEd Ex. 18.0, p. 7:148-51; Hill Sur., ComEd Ex. 45.0, p. 6:110-11. All data supporting the split balance sheets, including General and Intangible Plant accounts, were available to the parties for several months. *E.g.*, Hill Sur., ComEd Ex. 45.0, pp. 6:108-10, 8:166-68.

- In this Docket, ComEd had use of the CBMS system. CBMS is, and has been since January 1, 1998, ComEd's general ledger, and thus has been subject to three independent audits (as well as interim audit procedures). Hill Sur., ComEd Ex. 45.0, pp. 5:88-6:118. The restructured balance sheets are included in CBMS. *Id.*

ComEd's restructuring profoundly affected its costs. For example, in 1999, when ComEd owned generation, its fossil production expenses were 21.3% of its O&M Expenses; in 2000 they were just 0.16% of those expenses. Hill Sur., ComEd Ex. 45.0, p. 19:395-98.

The foregoing undisputed facts are at the heart of why ComEd is right about the functionalization of General and Intangible Plant. The actual restructured balance sheets, not arbitrary estimates, were used to determine the General and Intangible Plant used to provide distribution services. Because the balance sheets addressed all assets and liabilities of ComEd, including General and Intangible Plant, the only direct assignment or allocation that was necessary was in two areas: (1) removing the FERC-jurisdictional transmission component from the ComEd balance sheet, and (2) assigning or allocating the appropriate amount of General and Intangible Plant of Exelon BSC back to ComEd for ratemaking purposes. Hill Dir., ComEd Ex. 4.0 CR, App. A, pp. 1:20-2:25; Hill Sur., ComEd Ex. 45.0, pp. 8:170-9:175. Where necessary detail to assign General Plant items directly was not available, ComEd used an appropriate allocation factor. ComEd described in detail how General Plant costs in each account were assigned or allocated. Hill Dir., ComEd Ex. 4.0 CR, App. A, p. 9:176-81.

No party has submitted any evidence disproving any of the above facts, or identifying even a single inaccuracy in ComEd's assignment of General and Intangible Plant. Instead, some parties urge the Commission to use a general labor allocator because it used one to functionalize General Plant (not Intangible Plant) in Docket No. 99-0117. The Commission cannot base its decision here on its order in Docket No. 99-0117. That order is based on 1997, and is not *res judicata*. *E.g., United Cities Gas Co. v. Illinois Commerce Comm'n*, 163 Ill. 2d 1, 22-23, 643

N.E.2d 719, 729 (1994); *Mississippi River Fuel Corp. v. Illinois Commerce Comm’n*, 1 Ill. 2d 509, 513, 116 N.E.2d 394, 396-97 (1953).[†] Rather, the decision here must be based exclusively on the evidence in this record. 220 ILCS 5/10-103, 10-201(e)(iv); *Business and Professional People for the Public Interest v. Illinois Commerce Comm’n*, 136 Ill. 2d 192, 201, 227, 555 N.E.2d 693, 697, 709 (1989). That evidence reflects the very different state of the world in 2000 and strongly supports ComEd’s functionalization.

Staff’s Arguments Are Incorrect

Staff makes two overall assertions: (1) the Commission approved a labor allocator in Docket No. 99-0117, and ComEd offered no credible evidence to deviate from that approach; and (2) Staff’s particular labor allocator should be used because, Staff emphasizes, it includes the labor for both ComEd’s nuclear plants and the fossil plants sold to Midwest. Staff Br. at 7. Staff’s position would remove a huge amount, \$405,161,000 (with resulting upward adjustments of \$1,035,000 to accumulated depreciation and \$556,000 to ADIT), from ComEd’s net rate base. Staff. Br., App. A, Schs. 3, 4. Staff’s arguments are flawed, however, for multiple reasons.

First, ComEd submitted a wealth of evidence regarding its correct functionalization of General and Intangible Plant, including the evidence cited above and additional evidence. Hill Dir., ComEd Ex. 4.0 CR, pp. 1:19-23, 7:145-9:186 & Att. A; Heintz Dir., ComEd Ex. 14.0 CR, pp. 9:160-10:175, 16:288-21:385; Strobel Reb., ComEd Ex. 18.0, pp. 6:126-7:152; Hill Reb., ComEd Ex. 23.0 CR, pp. 4:87-9:183; Heintz Reb., ComEd Ex. 33.0, pp. 10:230-11:255; Hill Sur., ComEd Ex. 45.0, pp. 5:88-20:422, 19:400-20:422; Heintz Sur., ComEd Ex. 57.0,

[†] Indeed, while Staff criticizes ComEd here, Staff had no compunction in Docket 99-0117 about attacking nearly two decades of Commission decisions approving marginal cost ratemaking and now proposes in this Docket to extend embedded cost ratemaking to the remaining 90% of customers who still are on rates based on Commission-approved marginal cost principles. Staff Br. at 85-95; *see* Section II.F. Staff cannot have it both ways.

pp. 2:34-3:54; *see also* Hill Dir., ComEd Ex. 4.0 CR, pp. 17:345-18:369 & Att. B; Heintz Dir., ComEd Ex. 14.0 CR, pp. 21:387-23:452 (discussing functionalization of A&G expenses). ComEd's evidence addressed every individual General and Intangible Plant account, showing that they all are amenable to direct assignment and that the basis of the ruling in Docket No. 99-0117 -- that the costs there were not amenable to direct assignment -- is inapplicable here. Hill Sur., ComEd Ex. 45.0, pp. 7:148-10:213, 11:228-13:276; *Commonwealth Edison Co.*, No. 99-0117 (August 26, 1999), pp. 11, 27. In fact, Staff fails to identify a single General or Intangible Plant item that is not amenable to direct assignment, or that ComEd incorrectly functionalized. Staff's assertion that ComEd's functionalization "penalizes" delivery services ratepayers and shifts production expenses to jurisdictional rate base (Staff Br. at 13), is thus unsupported and circular -- that is, it assumes that Staff's general labor allocator is correct in order to argue for the allocator -- and false.

The Commission has made clear that it prefers direct assignment where feasible, because it inherently is more accurate. Hill Sur., ComEd Ex. 45.0, p. 7:138-46; *Commonwealth Edison Co.*, Docket No. 99-0013 (Oct. 4, 2000), pp. 44-45. Staff and IIEC have likewise supported direct assignment. Hill Reb., ComEd Ex. 23.0 CR, p. 5:108-10; Hill Sur., ComEd Ex. 45.0, p. 17:343-58; Chalfant Dir., IIEC Ex. 2.0 CR, p. 17:15-16; Chalfant Reb., IIEC Ex. 4.0 CR, p. 2:7-16. Staff witnesses testified in Docket No. 99-0117 that ComEd's functionalization of General and Intangible Plant was reasonable and should be adopted. Hill Sur., ComEd Ex. 45.0, pp. 11:224-26, 13:274-76; Lazare, Tr. 2802:4-22. Staff witness Bowers actually criticizes allocation where direct assignment is feasible. Hill Sur., ComEd Ex. 45.0, p. 17:354-58.

Staff's assertions that Mr. Hill's testimony is inconsistent are mistaken. Staff argues that Mr. Hill testified that the functionalization methodology used here was consistent with the labor

allocator used for General Plant in Docket No. 99-0117. Staff Br. at 8. He actually testified that ComEd consistently used direct assignment where feasible in both dockets. Here, ComEd used the better data now available to establish specific cost causation relationships to business activities. *E.g.*, Hill Reb., ComEd Ex. 23.0 CR, pp. 7:142-9:183; Hill Sur., ComEd Ex. 45.0, p. 15:308-24; Hill, Tr. 3546:21-3547:22. No party identified any flaw whatsoever in that effort. Staff's claim that Mr. Hill inconsistently explained the functionalization (Staff Br. at 8-9) is also wrong. Staff confuses ComEd with Exelon Energy Delivery Company, LLC, ComEd's immediate parent. Mr. Hill's redirect showed that Staff identified no inconsistencies, and Staff conducted no re-cross; yet Staff now ignores that testimony. Hill Dir., ComEd Ex. 4.0 CR, App. A, pp. 1:10-16, Hill, Tr. 3213:18-3218:14, 3548:15-3552:15; ComEd Redirect Ex. 92.

Also, Staff admits that the Commission did not use a general labor allocator for Intangible Plant in Docket No. 99-0117. While Intangible Plant much larger here, that does not matter. Lazare Reb., Staff Ex. 21.0, pp. 13:271-14:280. Moreover, ComEd's Intangible Plant consists of only five items -- generally large software systems -- supported by specific evidence. There was no contrary evidence. *E.g.*, Hill Sur., ComEd Ex. 45.0, pp. 11:228-13:276, ComEd Ex. 45.1; *accord* Hill Dir., ComEd Ex. 4.0 CR, p. 8:166-68 and App. A, p. 7:141-8:160.

Staff's position also is inconsistent with its approach in Docket No. 00-0802, where Staff insisted on a *pro forma* adjustment to reflect the sale of generation after the test year. *Central Illinois Public Service Co, et al.*, Docket No. 00-0802 (Dec. 11, 2001) ("*Ameren*"), p. 7. The Commission adopted Staff's position, which was uncontested. *Ameren* at 9. Here, Staff urges a labor allocator that includes generation not owned by ComEd, *i.e.*, fossil units sold before the test year. Indeed, Staff witness Bowers actually criticizes allocation where she contends direct assignment is feasible. Hill Sur., ComEd Ex. 45.0, p. 17:354-58.

Staff also argues that ComEd's functionalization methodology must be unreliable because the results differ from those in Docket No. 99-0117. Staff Br. at 10-11. That makes no sense. ComEd's functionalization of General Plant in Docket 99-0117 was rejected. Moreover, ComEd has been restructured since 1997, has directed its generation, has had an improved accounting data system (CBMS), and has restructured balance sheets that support more refined cost-causation allocators when direct assignment is not possible. In fact, Staff's analysis actually illustrates that ComEd's approach is more accurate. Hill Sur., ComEd Ex. 45.0, p. 18:374-88.

Staff also mistakenly argues that the restructuring did not take place until 2001, confusing the corporate formality of closing with the actual realignment of people, assets, and accounts, once again erroneously ascribing the confusion to Mr. Hill. Staff Br. at 13-15. Staff's claim that the restructuring occurred on January 1, 2001 is also irrelevant. The restructuring, which actually began in 2000 (1999, for the sale of the fossil units) plainly is known and measurable, and meets every possible criterion for such an adjustment. Indeed, Staff's position in *Ameren* is just that. Staff's position here also cannot be squared with its advocacy of *pro forma* adjustments in this Docket for alleged post-test year merger savings. Staff Br. at 57-63; *see* Section II.D.3.c.iv.

In addition, Staff argues that the Commission should base its decision on the use of labor allocators by "other Illinois utilities" in their cases. Staff Br. at 15-16. Another utility's choice, made for unidentified reasons, likely specific to that company's structure, costs and accounting, casts no doubt on ComEd's position. Nor is it evidence or authority here. Staff invites the Commission to make a decision that disregards the evidence and that would violate its legal responsibilities to set rates based on ComEd's costs, exclusively on the record.

Staff proposes to use not only a general labor allocator, but one distorted to include fossil units sold in 1999, thereby greatly inflating Staff's proposed adjustment. Staff Br. at 17-19. This is patently unreasonable. *E.g.*, Hill Sur., ComEd Ex. 45.0, pp. 5:88-13:276, 19:390-20:422 (having sold the entire fossil business in 1999, ComEd had no material A&G or General or Intangible plant costs related to that business in 2000). While Staff claims including the fossil plants is appropriate (Staff Br. at 17-19), it identifies no items functionalized by ComEd to jurisdictional rate base that do not belong there or that should be attributed to the fossil plants.[†] In addition, as noted above, Staff cannot credibly contend that its distorted "one size fits all" general labor allocator accurately reflects cost causation in this case. Even the other parties that propose a labor allocator, exclude the fossil plants. Staff Br. at 16.

Other Parties Arguments Are Incorrect

IIEC, which mixes up arguments regarding General and Intangible Plant and A&G expenses, offers four reasons for using a labor allocator to functionalize all of these costs: (1) the Commission used a labor allocator for General Plant and A&G expenses in Docket No. 99-0117; (2) these costs are not amenable to direct assignment; (3) ComEd did not use the same method for functionalization in prior bundled rate cases; and (4) FERC does not set transmission rates using the method employed by ComEd. IIEC Br. at 5-6.[†] None of IIEC's arguments has merit.

[†] Staff now also complains about ComEd's accounting for the fossil plant sale, which did not use the same labor allocator used in Docket No. 99-0117 for plant balance write-downs. Staff Br. at 17. There was no such objection in Docket Nos. 99-0273 and 99-0282 Cons. In any event, that a major real world transaction did not use an arbitrary labor allocator is no reason to use it here. As to the proceeds of the sale, the ability of ComEd to mitigate its stranded costs through the asset sales is entirely lawful just as are, *e.g.*, limitations on stranded cost recovery (the mitigation factor), large rate reductions, and the mandate of open access. ComEd's mitigating its stranded costs, too, is no reason to adopt Staff's proposed labor allocator.

[†] IIEC's mixture of General and Intangible Plant and A&G expenses is confusing, but understandable from a tactical perspective. IIEC emphasizes that a few specific costs -- it mentions "salaries of corporate officials and the cost of corporate offices" -- are not amenable to direct assignment (*e.g.*, IIEC Br. at 6), without identifying those few specific items as General Plant, Intangible Plant, or A&G costs. They in

Significantly, in the pending IP rate case, IIEC opposes use of the labor allocator for functionalization in light of its results given IP's restructuring. IIEC Init. Br., No. 01-0432, p. 8.

Their first three arguments actually are one composite argument. As discussed earlier, in Docket No. 99-0117, the Commission adopted a labor allocator because it found that the subject costs were not amenable to direct assignment. *Commonwealth Edison Co.*, Docket No. 99-0117 (August 26, 1999), pp. 11, 27. The Commission also found that ComEd had not made a "convincing argument" for not using a labor allocator as had been done in prior bundled rate cases. *Id.* Thus, because ComEd has shown that the costs in this Docket are amenable to direct assignment or, where not, have been correctly allocated using a superior allocator, all of IIEC's first three arguments fail. Indeed, when IIEC argues that ComEd's approach is not more accurate than its own, IIEC once again trots out the red herring of ComEd's Chief Executive Officer's salary. IIEC Br. at 9.

IIEC's arguments actually add nothing to Staff's arguments refuted earlier, except that, as noted above, IIEC points to prior ComEd bundled rate cases. IIEC Br. at 5, *et seq.* ComEd has shown that these arguments do not support the use of a labor allocator across the board, but only where direct assignment is not feasible and where that particular allocator appropriately reflects current cost causation. The labor allocator had little practical consequence in prior bundled rate cases, and its use then does not logically or factually support its use now. *E.g.*, Heintz Dir., ComEd Ex. 14.0 CR, pp. 9:160-10:175, 16:288-21:385; Hill Sur., ComEd Ex. 45.0, p. 12:220-23.

fact are A&G expenses. *E.g.*, Hill Sur., ComEd Ex. 45.0, pp. 15:305-16:326. IIEC also fails to quantify them. They actually are a small fraction of 1% of A&G. ComEd Cross Ex. 29. IIEC then chastises ComEd for directly assigning the costs, even though ComEd did not use direct assignment for these costs and instead used the very same labor allocator that IIEC wants to use for all the costs. Hill Sur., ComEd Ex. 45.0, pp. 15:305-16:326; Chalfant, Tr. 2556:22-2558:1. All of these tactics allow IIEC to cloud the issues and facilitate their attempt to have the tail wag the dog.

IIEC's final claim is that FERC supports the labor allocator. IIEC Br. at 9-10. Alan Heintz, former Section Chief in FERC's Division of Applications, debunked that claim, showing that it no longer reflects FERC's actions. Heintz Dir., ComEd Ex. 14.0 CR, p. 2:29-32; Heintz Reb., ComEd Ex. 33.0, p. 11:240-55; Heintz Sur., ComEd Ex. 57.0, pp. 2:34-3:54. On cross-examination, IIEC's witness acknowledged this. Chalfant, Tr. 2557:9-21. Moreover, even were FERC ardently committed to a labor allocator for transmission rates, that would not justify its use here, where direct assignment is feasible or a more accurate labor allocator is available. While the Commission is to defer to FERC as to FERC-jurisdictional rates, 220 ILCS 5/16-108(a), it is required to set distribution rates that allow ComEd full cost recovery and are cost based. 220 ILCS 5/16-108(c). The labor allocator does not do this.

GC offers nothing more than a desultory argument relying on the ruling as to General Plant in Docket No. 99-0117, asserting, utterly incorrectly, that: "ComEd presented no evidence that warrants the Commission deviating from the conclusion it reached barely more than two years ago." GC Br. at 26-27. The flaws in that argument were enumerated earlier. ComEd has submitted a mountain of detailed evidence, including account by account analyses. GC has not pointed to even one flaw in ComEd's analyses or one dollar of General or Intangible Plant that ComEd incorrectly functionalized.

Finally, the ARES Coalition's disingenuous attempts to bring suspicion on CBMS (ARES Br. at 13, 66-68, 70-71, 116) are unsupported, mischaracterize the testimony cited, and are wrong. Hill Sur., ComEd Ex. 45.0, pp. 5:88-6:118; *see also* Strobel Reb., ComEd Ex. 18.0, pp. 6:126-7:152; Gorniak, Tr. 1656:11-1661:21. Among other things:

The workpapers of the independent auditor review were made available to Staff during its field audit. At least five members of Staff were given a presentation on the CBMS system during their field audit. Staff has made no adjustments nor raised an issue regarding the integrity of CBMS data based on that review. At

least as important, the Company's accounts and records data that are verified and reviewed by an independent, world-class professional accounting firm is evidence that the data utilized in this proceeding from the CBMS system is both accurate and reliable.

Hill Sur., ComEd Ex. 45.0, p. 6:112-18. Indeed, all the underlying data were available to all parties for several months. *E.g., id.* pp. 6:108-10, 8:166-68.

In sum, Staff, IIEC, GC, and the ARES Coalition simply do not want to accept that the facts have changed since Docket No. 99-0117. There is no recognition of the changes that have occurred at ComEd with respect to General and Intangible Plant and A&G cost information since Docket No. 99-0117. Hill Sur., ComEd Ex. 45.0, p. 6:120-31. However, the Commission must base its decision exclusively on the evidence in the record. ComEd's functionalization is the only correct functionalization. The evidence will sustain no other conclusion.

3. Known & Measurable Changes to Test Year Plant Balances

ComEd properly and accurately made three proposed upward adjustments to distribution plant included in rate base. ComEd Br. at 45-46. ComEd was extremely conservative in making these adjustments, because it legally was entitled to seek upward *pro forma* adjustments for all rate base additions reasonably expected to be placed in service on or before the date of the Commission's order in this proceeding, or within 12 months of the initiation of this proceeding, which was filed on June 1, 2001. *Id.*

Staff and GC argue that the third adjustment, \$126,592,000 (gross figure), relating to plant placed in service in the second quarter of 2001, should be reduced to \$115,554,000, the amount ComEd actually had incurred or paid only as of June 30, 2001. Staff Br. at 20-22; GC Br. at 27-28. Their position is unwarranted and unfair. ComEd's proposed \$126,592,000 adjustment was based on the then estimated asset value (costs incurred and paid) at project completion, with ComEd noting that, as of the latest data then available, as of April 30, 2001,

ComEd had actually incurred or paid \$98,633,000. Voltz Dir., ComEd Ex. 5.0, pp. 13:269-14:300, ComEd Ex. 5.1. As Staff and GC agree, that figure reached \$115,554,000 by June 30, 2001. As of September 30, 2001, ComEd actually had incurred and paid \$123,680,000, and ComEd showed that because trailing expenditures would continue, the original figure of \$126,592,000 remained appropriate. Voltz Sur., ComEd Ex. 46.0, p. 2:26-42.

Staff's attack on Mr. Voltz's sworn testimony (Staff Br. at 21), is unwarranted, unfair, and specious. Staff suggests that testimony as to costs already incurred or paid is insufficient if not supported by other documentation, a position that is supported by no legal authority, and that goes far beyond the position regarding testimony as to expected costs that was recently reversed. *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 322 Ill. App. 3d 846, 751 N.E.2d 196 (2d Dist. 2001). Staff appears to assume that, once a project is placed in service, no additional costs will be incurred or paid. That assumption is supported by no evidence, is neither logical nor reasonable, and is contradicted by Mr. Voltz's testimony regarding trailing expenditures. Staff's reference to Mr. Voltz's "sudden claim" of costs from July through September 2001 in his surrebuttal filed on October 24, 2001 (Staff Br. at 21) overlooks, among other things, that ComEd's rebuttal was filed on September 20, 2001, when not all of that data were available, and that Staff first advocated the adjustment in its rebuttal filed on October 16, 2001. GC offers no relevant rationale for its assertion that ComEd should include only costs incurred or paid as of June 30, 2001. GC Br. at 27-28. Also, its assertion that "ComEd should not earn a return on investments that it has not made" (*id.* at 28) overlooks the scope of ComEd's legal entitlement referred to above. In any event, ComEd plainly is entitled to recover the \$123,680,000 in costs actually incurred and paid through September 30, 2001. Voltz Sur., ComEd Ex. 46.0, p. 2:40-42.

4. Other Adjustments to Rate Base (Non-Plant)

a. Budget Payment Plan Balances

Staff proposes to reduce rate base by \$165,000, claiming this represents the 13-month average total of customer budget payment plan balances, which therefore represents cash working capital available for ComEd's use. Staff Br. at 19-20. Budget payment plan balances are customer receivables and liabilities that affect ComEd's cash working capital requirements. Hill Reb., ComEd Ex. 23.0 CR, p. 14:300-12. Staff acknowledges that cash flows from budget payment plan balances may be considered a component of cash working capital. ComEd did not seek a working capital component of rate base in this case. *Id.* Because the payment plan balances constitute just one component of working capital, to single out this issue and make an adjustment is unreasonable, and inconsistent with the Commission decision in *Ameren* (at 4).

b. Accumulated Deferred Income Taxes

See Section II.C.4.b of ComEd's Initial Brief. Section II.C.7, *infra*.

5. Plant Adjustments

a. Plant Expenditures for Q2 2001

This subject is addressed in Section II.C.3, except for GC's baseless proposal to increase by \$90,226,000 ComEd's accumulated depreciation and amortization (also referred to as depreciation reserve) for Distribution Plant, a subtraction from gross Distribution Plant. GC Br. at 28-29.

- GC asserts that the adjustment is appropriate based on ComEd's *pro forma* adjustment for certain distribution plant placed in service in the second quarter of 2001. ComEd in its direct case already made the correct additions to depreciation reserve for that plant. Hill Dir., ComEd Ex. 4.0 CR, pp. 23:486-24:503 & App. C, Sch. B-2.2; Hill Reb., ComEd Ex. 23.0 CR, p. 32:714-16; Hill Sur., ComEd Ex. 45.0, p. 34:725-29. GC acknowledges that ComEd's adjustment is correct. Effron Dir., GC Ex. 2.0, p. 40:5-8.
- GC's proposal ultimately amounts to an unjustified and erroneous attempt to use the depreciation reserve as of June 30, 2001, for all jurisdictional distribution plant, instead of

using the figure as of December 31, 2000, adjusted for the impact of the *pro forma* adjustment made in ComEd's direct case. The jurisdictional depreciation reserve for distribution plant is the cumulative depreciation for all such plant. GC incorrectly ascribes the entire increase in the accumulated depreciation reserve for distribution plant from December 31, 2000, to June 30, 2001, to all distribution plant additions during this six month period, resulting in a massively inflated adjustment, far larger than the correct amount already reflected in ComEd's direct case. Hill Reb., ComEd Ex. 23.0 CR, pp. 32:704-33:727; Hill Sur., ComEd Ex. 45.0, pp. 33:717-34:742.

- GC's error is clearly evident from Effron Reb., GC Ex. 5.0, GC Ex. 5.1, Sch. DJE-6.2. GC assumes that a \$372,098,000 increase in distribution plant over that six month period leads to the \$144,732,000 increase in depreciation reserve over this same period by virtue of the adjustment percentage used to calculate its depreciation reserve adjustment. Effron Reb., GC Ex. 5.0, GC Ex. 5.1, Sch. DJE-6.2. However, a simple calculation of the resulting depreciation rate for this reserve adjustment for additions during that six month period is 38.9%, or an annual depreciation rate of 77.8% for these additions. That is absurd on its face. The correct annual depreciation rate for high voltage distribution plant is 2.4% and for other distribution plant is 3.6%. Hill Dir., ComEd Ex. 4.0 CR, App. C, Sch. B-2.2. The depreciation reserve adjustment of \$90,226,000 proposed by GC actually can only be an improper test year change to a June 30, 2001, accumulated depreciation reserve amount for all jurisdictional distribution plant. Hill Reb., ComEd Ex. 23.0 CR, p. 32:704-17; Hill Sur., ComEd Ex. 45.0, pp. 33:717-34:742.
- Finally, GC's figure adjustment is incorrect based on its own witness' spurious calculations. It would be \$89,906,000. Effron Reb., GC 5.0, GC Ex. 5.1, Sch. DJE-6R.

b. Proposed Retired Plant

ComEd agrees with Staff's proposed adjustment here, which has no net effect on rate base. ComEd Br. at 47; Staff Br. at 22 & App. A, Sch. 4, p. 1.

**c. Retirements Related to 2001
Replacement Plant**

ComEd agrees with Staff's proposed adjustment here, which has no net effect on rate base. ComEd Br. at 48; Staff Br. at 22-23 & App. A, Sch. 4, p. 1.

**d. Accumulated Depreciation
Adjustment Related to Overtime
and Alleged Premiums Paid**

There is no basis for this adjustment. See Section II.C.6.

**e. Accumulated Deferred Taxes
Adjustment Related to Overtime
and Alleged Premiums Paid**

There is no basis for this adjustment. *See* Section II.C.6.

**6. Prudence of Distribution
Capital Investment Costs**

a. Effect of Alleged Imprudence on Rates

Focusing on whether particular distribution capital projects could or should have been built earlier is the regulatory equivalent of Much Ado About Nothing. When capital investments are made, and whether test year capital investments are representative of expenditures in other years, make no difference in setting rates. Unlike O&M expenses, all capital expenditures made prior to and during the test year are reflected in a utility's revenue requirement. ComEd Br. at 51. Had ComEd made certain additions to Distribution Plant earlier, those expenditures would simply have been included in rates sooner. Helwig Reb., ComEd Ex. 19.0, pp. 6:117-7:141; Helwig Sur., ComEd Ex. 43.0, p. 3:49-52; ComEd Br. at 51.

Some intervenors also criticize ComEd witnesses' prudence analysis, implying that if certain distribution capital expenditures could or should have been completed earlier, those project expenditures were *per se* imprudent, and should therefore be excluded from ComEd's jurisdictional revenue requirement. GC Br. at 32-33. It is intervenors, not ComEd, who apply a prudence standard that deviates from the statutory definition. Whether an investment is prudent, for purposes of inclusion in rate base, is defined by Section 5/9-212 as follows:

“[P]rudent” means that at the time of certification, initiation of construction and each subsequent evaluation of any construction project until the time of completion, based on the evidence introduced in any hearings and all information which was known or should have been known at the time, and relevant planning and certification criteria, it was prudent and reasonable to conclude that the generating or production facility would be used and useful in providing service to customers at the time of completion.

220 ILCS 5/9-212. (emphasis added). Additions to ComEd's Distribution Plant are properly included in rate base if such additions are found to be prudent at the start of construction, and used and useful in providing service to ComEd's customers at the time of completion. 220 ILCS 5/9-211, 9-212. Attempts to judge prudence through the benefit of hindsight analysis, as certain intervenors do, are illegal. Moreover, concluding that something could have been built earlier does not equate to imprudence. Helwig Reb., ComEd Ex. 19.0, pp. 7:149-8:170. The evidence overwhelmingly demonstrates that ComEd's distribution capital expenditures were prudent, are used and useful, included no unnecessary costs attributable to "failures of the past," and are properly included within ComEd's rate base. ComEd Br. at 49-60.

b. Prudence of Specific Distribution Capital Investments in Rate Base

Overwhelming evidence supports ComEd's additions to Distribution Plant included in jurisdictional rate base. ComEd Br. at 49-53. ComEd's Initial Brief described specific testimony from experienced ComEd employees, expert in their fields, who explained that the costs of all Distribution Plant additions were prudent and reasonable. Moreover, the initial brief outlined the specific steps taken by ComEd's witnesses to support their testimony that the costs of additions to Distribution Plant were prudent and reasonable.

Nonetheless, GC argues that deferred capital investments and maintenance of ComEd's distribution system necessitated an accelerated "catch up." It speculates that such "catch up" must have produced additional costs, which it cannot identify. GC Br. at 29-33. GC also speculates that past overloading of portions of ComEd's distribution system may have led to either premature retirement of distribution equipment or failure of distribution equipment. GC Br. at 33-35. It then claims that the costs, if any, of replacing this hypothetically-damaged equipment are unreasonable costs that cannot be included in Distribution Plant. GC Br. at 35-36.

GC's arguments lack support in the record. They also completely lack specificity since GC fails to identify a single transformer, substation, line, or other construction project that ComEd seeks to add to Distribution Plant as being the subject of either some increment of imprudent "catch up" costs or failure due to overloading.

In an attempt to deflect the Commission from the lack of evidence in this record in support of its argument, GC argues that the Commission should give no weight to ComEd's testimony on this issue. GC boldly claims: "The only thing Edison offers is a collection of conclusory opinions from its witnesses, and none of those witnesses' opinions were based on quantitative data." GC Br. at 8. GC is wrong.

General Claims of Increased Costs Resulting From Mismanagement Are Flawed

ComEd's evidence discloses a detailed look at the major projects that its seeks to add to Distribution Plant. The examination was made by experts. Dr. James B. Williams, ComEd's Vice President, Project and Contract Management, has responsibility for directing all ComEd's construction activities, and has 23 years of experience in engineering and construction of capital facilities. Williams Reb., ComEd Ex. 25.0 CR, pp. 1:1-6, 1:13-2:21. David G. DeCamppli, Exelon Energy Delivery's Vice President of Engineering and Technical Analysis, also has years of experience with the operation, maintenance, and construction of distribution system facilities for a variety of utilities. DeCamppli Dir., ComEd Ex. 6.0, pp. 1:1-8, 1:19-3:56. Other witnesses with long experience in the utility business supported various aspects of these witnesses' testimony on the prudence of additions to Distribution Plant. Contrary to GC's wholly unsupported contention, Dr. Williams and Mr. DeCamppli did not submit biased conclusory statements devoid of analysis or specificity.

In fact, substantial detail is contained in the record. For example, Mr. DeCamplic identified five key projects (LaSalle, Diversey, Ohio, Northwest and North Huntley) completed during what GC refers to as ComEd's "two year recovery program." DeCamplic Dir., ComEd Ex. 6.0, p. 15:311-19, ComEd Ex. 6.1. The five projects analyzed involved \$171,352,000 in total proposed additions to Distribution Plant. ComEd Ex. 6.1. Each was described in great detail. Major work was identified. The reasons for the project were provided. The results of the projects were explained. The costs of the projects were identified. The particular transformers added or ring buses installed were detailed. *Id.* All of this was done by Mr. DeCamplic as a foundation for testimony that the cost of these facilities was reasonable, prudent, and not inflated. DeCamplic Dir., ComEd Ex. 6.0, pp. 17:367-18:389; DeCamplic Reb., ComEd Ex. 26.0 CR, p. 6:156-72. In similar fashion, Mr. DeCamplic set out the 24,308 new poles ComEd added to Distribution Plant. He identified the 2,600 miles of overhead conductors, 4,550 miles of underground cables and 19,121 distribution transformers added between 1997 and 2000, as well as numerous other upgrades, replacements and additions to existing substations.

Against this background, Mr. DeCamplic and Dr. Williams both testified that the additions to Distribution Plant since 1997 were necessary to meet ComEd's obligation to offer and provide delivery services at an acceptable level of reliability. They both testified that the additions were used and useful and installed at a cost that was reasonable and prudent. ComEd Br. at 49, 51. Both witnesses expressed these conclusions after an extensive process. As Mr. DeCamplic described in his testimony at the hearing, his analysis began by reviewing each of the contracts entered into by ComEd for construction of each of the major additions to Distribution Plant. Thereafter, he questioned the project's managers to develop a full understanding of the scope, nature and cost of the project. He compared total projects costs at each project to other projects,

but determined that the major projects were all “quite unique.” DeCampli, Tr. 1430:7-10. Based upon that determination, in Mr. DeCampli’s words he “had to take that particular project apart.” DeCampli, Tr. 1430:10-18. Mr. DeCampli explained that this meant looking at material acquisition costs, use of overtime, use of contracts and construction strategy in order to ascertain whether or not each of those contracts was “in fact, a prudent investment.” DeCampli, Tr. 1430:13-18. His analysis also assessed “the amount of new growth going on in ComEd territory in the way of housing starts and new additions.” DeCampli, Tr. 1439:22-1440:6. Based upon all this work, Mr. DeCampli concluded: “[Y]es, it absolutely is. It’s a very unique piece of work done in a unique city, and I believe it was done quite well.” Tr. 1430:19-21. This same approach was followed by DeCampli for each of the five major projects and each was “evaluated in great scrutiny.” DeCampli, Tr. 1431:4-6.

Contrary to GC’s unsupported assertions, ComEd’s analysis of these projects was also based upon quantitative data. For example, Mr. DeCampli testified that his analysis went down to the level of specific project component cost. DeCampli, Tr. 1430:10-18. One of the major components in ComEd’s projects that are proposed to be added to Distribution Plant is transformers. GC, in fact, argues that ComEd bought out complete factories of transformers and, presumably, overpaid to do so. GC Br. at 22. Yet, ComEd empirically studied all transformer purchases during the time period 1998 to 2000. There were no significant incremental costs for expedited manufacture in connection with the fifty-nine 138 kV transformers it purchased during that time period. ComEd Br. at 56-57. Based upon the analysis contained in the record, three different types of 138 kV transformer were surveyed. One type maintained a fixed price throughout the entire 1998-2000 time period. The other two, even during the time period ComEd was supposedly buying out entire factories of capacity, increased in cost only slightly.

Prices increased between 1998 and 1999 between 4.9 and 6.8% depending on transformer type. In 1999, the year ComEd began its two year recovery program, prices only increased 2.2 to 2.3%. Voltz Reb., ComEd Ex. 24.0 CR, p. 8:147-61. The hard statistical evidence simply does not support GC's speculative arguments.

ComEd Did Not Pay "Premiums" to Contractors

Dr. Williams also scrutinized ComEd's major projects. Based upon 20 years of experience in the construction business and his review of one or two major requests for proposal every week for the last ten years, he concluded ComEd did not overpay in connection with his major projects. Williams, Tr. 860:16-861:6; Williams Reb., ComEd Ex. 25.0 CR, p. 5:96-99. Dr. Williams whether ComEd paid premiums to get its major projects done early, and he placed in context the overall construction schedule for the major projects.

As to the schedule, GC contends that Dr. Williams testified before the Commission that the major projects it now seeks to add to Distribution Plant set "world records in design and construction" and therefore, according to GC's reasoning, must have set world records for prices. As Dr. Williams testified, that is not true, and the quotation is taken out of context. Williams Sur., ComEd Ex. 47.0, pp. 1:15-2:27. The project schedule for these major projects was never accelerated. Nor was the time to perform the work reduced by the payment of incentives. *Id.*, p. 2:36-39. Instead, a properly incentivized contractor performed complicated, unique work on a streamlined basis within ComEd's historical project schedule. *Id.*, p. 2:28-36. The work schedule was made possible by a combination of good weather permitting excavation and foundation work during the winter season and unprecedented levels of cooperation from the City of Chicago during the permitting process. *Id.* While the unique work was done in a timely

fashion, Dr. Williams convincingly testified that no premium was paid to any contractor in order to get the work done. Tr. 838:20-839:15; ComEd Br. at 55-56.

On the subject of premiums, Dr. Williams distinguished between an overpayment as compared to market price for a project and a typical time-based incentive designed to shift the economic risk of not meeting a completion date from the owner to a contractor. ComEd Br. at 55-56. He explained that in negotiating with its prime contractor, ABB, for the major projects that ComEd now seeks to add to Distribution Plant: “[W]e negotiated hard with them on price.” He expressly stated, “Price was heavily weighted. Price is always heavily weighted, and we endeavor to drive the price as low as we can while getting the quality that we need.” Tr. 859:14-860:15. He concluded, based on his experience, that no overpayment was involved. Tr. 860:16-861:3. He explained that the use of contract incentives, including time related incentives, represented “pay for performance.” It transferred of risk from ComEd to its contractor in the sense that if timely completion is not achieved, the contractor will experience lower overall compensation. ComEd Br. at 55. He further described his own experience in the construction industry with time-related incentives. Williams, Tr. 861:4-6. In short, such incentives are a part a contractor’s entire compensation package, not premiums on top of what the contractor ought to have been paid under market conditions.

ComEd Executive Vice President David R. Helwig also specifically addressed these major projects. Mr. Helwig provided a detailed professional assessment of the nature, cost, reasonableness and even reasons for construction of the projects. He specified that much of the new investment was actually made in response to unanticipated load growth, not past imprudence. For example, he noted that of the major projects in the City of Chicago, LaSalle, Diversey, and at least a portion of the Northwest project were specifically built for capacity

purposes. Helwig, Tr. 2624:16-18. He explained the distinction between replacement of switch gear for purposes of reliability and addition of transmission capacity at the 138 kV level in the downtown area to support load growth that had “subsequently developed.” Helwig, Tr. 2625:6-2626:11. Mr. DeCampli confirmed this testimony. He pointed out that ComEd’s net peak weather adjusted system load increased 3.9% and 4.2% during the years 1998 and 1999, a number that was double the historic average over the prior 7 years. DeCampli, Tr. 1432:4-10. As Mr. DeCampli testified, this doubling of anticipated load translates into a requirement for construction of five more substations (of ComEd’s most utilized type) at some location in ComEd’s system. DeCampli Sur., ComEd Ex. 48.0, p. 5:100-14. This sharp increase in demand contributed substantially to the reasonable and prudent construction of ComEd’s major proposed additions to Distribution Plant.

In contrast, GC witness Schlissel conceded he made no project by project analysis in order to distinguish between the prudent cost of a sustained planned maintenance program and the imprudent cost of “catch up”. Schlissel, Tr. 2196:21-2197:3. In fact, Mr. Schlissel could not even describe in his testimony a methodology that could be used for such an analysis. Nor could he identify one ComEd document that identified a project cost that would not have been incurred, but for past imprudence. Schlissel, Tr. 2222:9-2224:6. Similarly, GC witness Effron testified that he performed no analysis or study whatsoever of which plant, substation, or line he thought might have involved enhanced or inflated cost due to imprudence. Effron, Tr. 2106:9-15. Nor could he tell the Commission to what extent the cost of Distribution Plant additions were necessary to deal with unanticipated load growth. Effron, Tr. 2106:2-8. Finally, GC’s Mr. Bodmer acknowledged that he expressed no opinion whatsoever about the five major distribution projects analyzed in detail by Mr. DeCampli and Dr. Williams; the prudence of

ComEd's additional 24,308 new distribution poles; the 2,600 additional miles of distribution overhead conductors, ComEd's 4,550 miles of underground distribution cables; or ComEd's 19,121 added distribution transformers. Bodmer, Tr. 1846:18-1849:1. In fact, he conceded that he expressed no opinion about the prudence or cost of any individual distribution capital project performed by ComEd after 1997. Bodmer, Tr. 1849:2-1850:9.

Not only did GC's witnesses fail to provide any support for the argument that ComEd overpaid for additions to Distribution Plant, but GC speculates wildly about the potential cost of past overloading to ComEd's Distribution System. GC Br. at 35. GC confidently claims "overloading the system may lead to premature retirement of distribution equipment, thereby generating excess costs." The contention is wholly without record support and based upon speculation in several respects.

GC presented absolutely no scientific evidence of the amount, nature or impact of overloading upon transformers or other distribution system components. The entire GC argument relies on absolutely no evidence from its own witnesses. Instead:

- GC starts with a single reference to ComEd's "Blueprint for Change" which indicates that in Summer 1999 "certain" substations were overloaded at times of "peak summer demand." From that quotation GC jumps to an unsupported conclusion. Mr. Helwig was asked whether the useful life of equipment loaded beyond emergency ratings would be shortened. Mr. Helwig answered that it would depend on how high each individual piece of equipment was loaded and for how long. Helwig, Tr. 2652:18-2653:8.
- GC next tries to suggest that degradation of support systems for distribution equipment could shorten the useful life of such equipment. Again the point never rose above the level of speculation. Mr. Helwig carefully explained that whether a degradation of support systems could damage equipment or shorten its useful life would depend upon a wide variety of factors including the specific conditions applicable during a given time period to a given piece of equipment. Helwig, Tr. 2655:1-12.

In short, on the subject of overloaded equipment leading to excessive costs GC has built its arguments from a house of cards. It has no evidence, no study, and no testimony to suggest that any amount was spent by ComEd to replace imprudently overloaded equipment.

In fact, the record shows to the contrary. No significant amount of money was spent replacing degraded equipment due to overloading in connection with the five major projects described by Mr. DeCampli. Those were expansion projects designed to increase flexibility and meet unexpected additional demand. The record makes it clear that the major projects involved increased capacity, the installation of additional transformers, the installation of a new ring bus, and other features all designed to increase key substation reliability and prevent overloads. DeCampli Dir., ComEd Ex. 6.0, ComEd Ex. 6.1.

GC also contends that “the Company did chose not [sic] to track the costs of its errors.” GC Br. at 30. GC mischaracterizes the testimony of ComEd’s witnesses and once again leaps to unsupportable conclusions. Mr. DeCampli indicated that ComEd could track a particular desired category of costs, but that assumes that a readily defined category exists. DeCampli, Tr. 1423:19-1424:1. Mr. Helwig also agreed that ComEd’s accounting system would have been capable of tracking costs identified as being caused by inadequate maintenance, if accounts had been set up with that structure. Helwig, Tr. 2664:3-9. However, Mr. Helwig pointed out that ComEd has never tracked costs that way. It creates accounts by work activity or project. Helwig, Tr. 2664:10-16. Accordingly, ComEd’s accounting system can pull up detailed information based upon a number of different fields or identifying terms, such as running queries by project, contractor, equipment component, etc. Projects and equipment are not tracked by rationale because, as was explained during the course of this Docket, a particular project is never undertaken for a single reason. DeCampli, Tr. 1423:8-1424:1. Further, because projects evolve and change over time, attributing particular expenditures as “catch-up” costs rather than ordinary course expenditures based upon when they occurred is simply not possible. DeCampli Sur., ComEd Ex. 48.0, p. 7:147-59. Nonetheless, the simple fact remains that, even if a category of

“catch up” costs existed, a query would show its total expenditures as zero. It is for these reasons that ComEd could not provide quantifications of the amount of alleged “catch up” costs, or the precise costs of its two-year recovery program that were included in its test year revenue requirement. ComEd did not shirk its discovery responsibilities or deliberately structure its accounting system to obscure costs.

In sum, GC’s argument that the two year recovery program simply reflects “catch up” from past imprudence cannot be sustained. The specific and detailed testimony of Mr. DeCampli, Dr. Williams and Mr. Helwig must be contrasted with the testimony of GC’s witnesses. They made conclusory claims, not ComEd’s witnesses. They contended there must have been imprudent cost inflation associated with ComEd’s two year recovery program without analysis, not ComEd’s witnesses.

ComEd’s Capitalized Overtime Was Reasonable

In addition to the general arguments discussed above, Staff recommends that ComEd’s recovery for capitalized overtime be limited to a more normal work schedule. Staff Br. at 32. Ironically, Staff proposes to limit recovery of ComEd’s capitalized overtime expenditures to 1998 levels, a time in which Staff indicates that ComEd’s “primary criterion for distribution expenditures was to minimize cost” (Staff Br. at 27), causing ComEd’s distribution system to “degrade and become unreliable.” Staff Br. at 32. No party indicated that 1998 expenditures levels are consistent with “normal” spending levels of a high reliability distribution company. Nor is there any evidence that additions to Distribution Plant were performed in anything but a controlled manner. In fact, ComEd’s project management practices for those projects were more efficient than past practices, and have since been adopted for future major distribution projects,

whenever possible. ComEd Br. at 54. ComEd would have experienced no cost savings on overtime had the work performed in 1999-2001 been performed any earlier. ComEd Br. at 58.

ComEd Should Recover Its Costs

Staff's continued comparison of the situation that existed in the aftermath of the 1999 heat wave to the public safety crisis resulting from faulty gas lines in the *CILCO* case is inappropriate. While ComEd is not attempting to minimize the seriousness of the failures of its distribution system in 1999, no falsification of maintenance documentation was involved. DeCampli Reb., ComEd Ex. 26.0 CR, pp. 10:242-11:267. Moreover, in *CILCO* the utility presented no evidence on the subject of imprudent "catch up" costs. As discussed above, ComEd's evidence that no "catch up" costs caused by imprudence are contained in proposed additions to Distribution Plant is both extensive and largely unrefuted.

The ARES Coalition suggests that ComEd somehow "hid the ball" regarding costs incurred as a result of imprudence or mismanagement -- first claiming that ComEd presented Staff with unusable information, and then insinuating that ComEd officers had promised that ComEd would be making adjustments to its revenue requirement for past imprudence or mismanagement. Both of those claims are meritless and distortions of the evidence. The ARES Coalition states that ComEd did not provide information to Staff in a form that allowed Staff to perform an audit, implying that ComEd intentionally obstructed Staff's review of ComEd's distribution expenditures, a veiled accusation that Staff witness Gorniak acknowledged was not the case. Mr. Gorniak indicated that ComEd's new information system, CBMS, did not provide a paper general ledger but, rather, produced information based upon queries posed by the operator. Gorniak, Tr. 1661:3-12. ComEd never prevented Staff access to any information contained in the system. Gorniak, Tr. 1661:17-19. ComEd has provided Staff and other parties

access to all of its documentation regarding its distribution capital projects -- over 30,000 pages providing specific details of each major project, including project justification, project schedules, contract price, and contract terms and conditions. Williams Sur., ComEd Ex. 47.0, pp. 5:103-6:127. Other parties' witnesses simply failed to review that detailed material and, in lieu of their own review and analysis, now seek to substitute an audit, after the record in this case is already marked "heard and taken."

The ARES Coalition erroneously implies that statements by Ms. Strobel and Ms. Juracek constitute a ComEd commitment to affirmatively make adjustments for imprudence or mismanagement, and that ComEd failed to do so. Ms. Strobel correctly stated that ComEd has not included in its revenue requirement any costs that were higher because of failures of the past (Strobel Reb., ComEd Ex. 18.0, p. 6:117-24), and Ms. Juracek noted that ComEd has not inflated its revenue requirement in this Docket. Juracek Dir., ComEd Ex. 1.0, p. 19:480-84. Both statements are accurate, and consistent with ComEd's filing and the evidence presented in this Docket. Neither statement can be reasonably construed as a promise to make a particular adjustment. The ARES Coalition's attempt to twist these statements does not change the facts that ComEd's revenue requirement is supported by voluminous evidence in the record demonstrating the prudence of such costs, the fact that such projects are used and useful, and that ComEd's careful review of the projects underlying its distribution capital and O&M projects reveals that its costs are consistent and reasonable for such projects.

**c. Request for Audit of New Distribution
Capital Investment Costs**

Certain intervenors and Staff propose that the Commission launch an audit of ComEd's transmission and distribution expenditures, ignoring the voluminous evidence produced during the course of this Docket as well as the legal prohibitions against such an undertaking. An audit

is wholly unnecessary in that ComEd's distribution expenditures were demonstrated to have been prudent, and used and useful. The following evidence, largely uncontested, supports ComEd's proposed jurisdictional revenue requirement in this Docket:

- ComEd's distribution projects are used and useful, and support the reliable delivery of electric power and energy to ComEd customers (ComEd Br. at 49);
- ComEd has proper accounting procedures and internal checks to guard against overpayment on distribution projects (ComEd Br. at 53);
- ComEd's distribution expenditures are subject to annual review by independent auditors (DeCampli Reb., ComEd Ex. 26.0 CR, p. 2:48-55);
- ComEd's distribution expenditures are detailed on FERC Form 1, filed annually with FERC, and accessible to public review (DeCampli Reb., ComEd Ex. 26.0 CR, p. 2:48-49, 52-54);
- ComEd analyzed costs of major projects on a project-by-project basis, and determined that no additional costs were paid to contractors in the form of premiums (ComEd Br. at 55-56);
- ComEd disaggregated project components, such as transformers and other equipment, revealing that ComEd's expenditures were not significantly above costs paid in previous years and were, in fact, consistent with prevailing market rates for the time (ComEd Br. at 56);
- There would have been no differential labor costs had ComEd performed certain capital distribution projects at an earlier point in time (ComEd Br. at 58);
- ComEd provided intervenors with over 30,000 pages of documents describing every aspect of ComEd's capital distribution projects, including project justifications, selection of vendors, schedules, and terms and conditions of contracts (Schlissel, Tr. 2202:11-16, Williams Sur., ComEd Ex. 47.0, pp. 5:103-6:127); and
- Any post hoc audit differentiating prudent distribution plant additions from imprudent "catch up" costs will be unscientific, filled with approximations and largely driven by the assumptions selected by the auditor chosen.

There are also a variety of legal reasons why intervenors' requests for an audit must be rejected, which are addressed more fully in Commonwealth Edison Company's Reply In Support Of Motion To Dismiss Petition For Investigation And Audit (Docket No. 01-0664):

- The Act permits audits pertaining to rates that are currently being charged, and does not permit audits for the purpose of examining prospective rates (Juracek Reb., ComEd Ex. 20.0, p. 38:891-903);
- The Act contemplates rate case audits only for nuclear generating facilities (DeCampli Reb., ComEd Ex. 26.0 CR, p. 13:317-29);

- Intervenor’s audit request amounts to an unlawful collateral attack on a pending proceeding (this Docket);
- Intervenor’s audit request seeks to unlawfully set rates based upon matters other than the evidentiary record in this Docket; and
- Interim rates imposed as a by-product of any audit proposal are prohibited by the Act and outside the Commission’s authority.

7. Other Rate Base Issues

GC proposes a \$101,585,000 reduction to operating reserves deducted from plant in service, and another \$40,230,000 adjustment to accumulated deferred income taxes (“ADIT”) relating to operating reserves. Both adjustments hinge entirely on Mr. Effron’s proposed labor allocator for A&G expenses (Effron Dir., GC Ex. 2.0, pp. 44:14-28), which is fundamentally flawed. *See* Section II.D.3.b; Hill Reb., ComEd Ex. 23.0 CR, pp. 30:666-31:673.

D. Operating Revenues and Expenses

ComEd’s initial proposed jurisdictional operating expenses were \$1,267,842,000, plus appropriate incomes taxes. Given the downward adjustments that ComEd made or agreed to its rebuttal and surrebuttal testimony, its revised proposed jurisdictional operating expenses are \$1,240,297,000. ComEd Br. at 62. Setting aside Staff’s erroneous downward adjustments in the net amount of \$60,002,000, based on its proposal to use a crude, less accurate general labor allocator to allocate A&G expenses (*see* Section II.D.3.b), ComEd’s revised proposal is only 4.82% higher than Staff’s revised proposed jurisdictional operating expenses of \$1,183,234,000. Staff Br., App. A, Schs. 1, 2. ComEd’s jurisdictional operating expenses are prudent and just and reasonable.

1. Recommended Operating Income Statement

See Section II.D.1 of ComEd’s Initial Brief. ComEd Br. at 62.

2. Operating Revenues

See ComEd Br., Section II.D.2, Section I.C.1 (discussing costs borne by ComEd's shareholders and the "lost revenues" calculations, GC CX Ex. 63 (GC Br. at 43-46)).

3. Operating Expenses

a. Functionalization of Generation, Transmission, and Distribution Expenses

ComEd correctly functionalized its operating expenses, as well as the associated depreciation and amortization expenses and taxes other than income taxes. ComEd Br. at 17-18, 63-65. ComEd's functionalization of A&G expenses in general and certain other particular expenses is addressed in Sections II.D.3.b and II.D.3.d.

The ARES Coalition asserts that ComEd functionalized to the distribution function certain operating expenses that should be classified as "supply" (a/k/a generation or production) costs, suggesting that ComEd has "refunctionalized" to distribution \$66.5 million of operating expenses that were functionalized as supply costs by the Commission in Docket No. 99-0117, consisting of (1) \$39.5 million of incentive compensation included in distribution O&M and (2) \$27 million of O&M refunctionalized to distribution in accordance with the FERC "seven factor" test. ARES Br. at 13, 59, 65-66, 69-70, 90. That is false, for several reasons.

- The overwhelming and uncontradicted evidence shows those costs are correctly functionalized; jurisdictional distribution costs; there is no contrary evidence, just the ARES Coalition's unsupported innuendo. *E.g.*, Voltz Dir., ComEd Ex. 5.0, pp. 5:86-6:116, 16:332-38, 17:354-65 (all distribution O&M); DeCampli Dir., ComEd Ex. 6.0, pp. 19:408-23:480 (all distribution O&M); Hill Reb., ComEd Ex. 23.0 CR, pp. 28:610-29:43, 34:751-98; Juracek Reb., ComEd Ex. 20.0, p. 43:1015-16; Hill Sur., ComEd Ex. 45.0, pp. 22:474-23:513. The ARES Coalition's misleading and inaccurate comments about ComEd's CBMS system (ARES Br. at 13, *et seq.*) are refuted in Section II.C.2.
- None of those costs ever was recorded as a supply cost. In Docket No. 99-0117, and through 1999, the corresponding incentive compensation expenses were recorded in FERC Accounts 920-921, which are A&G Accounts, not supply Accounts. *E.g.*, Hill Reb., ComEd Ex. 23.0 CR, pp. 34:751-35:777; Hill Sur., ComEd Ex. 45.0, pp. 22:474-77, 23:492-506. As the ARES Coalition knows, the challenged \$27 million in O&M expenses were

refunctionalized from FERC transmission Accounts, not supply Accounts, to distribution. *E.g.*, ARES Br. at 13; Hill Sur., ComEd Ex. 45.0, pp. 22:474-23:491.

- The ARES Coalition has mischaracterized the rulings in Docket No. 99-0117. In that Docket, the Commission allocated all A&G costs among the supply, transmission, and distribution functions using a general labor allocator -- it did not hold that all A&G costs in general, or incentive compensation costs in particular, were supply costs. *Commonwealth Edison Co.*, Docket No. 99-0117 (August 26, 1999), p. 27. The Commission made no ruling even remotely implying that refunctionalized transmission O&M costs were supply costs.
- The ARES Coalition misleadingly omits that only \$41 million of the challenged \$66.5 million is included in ComEd's revised proposed revenue requirement. ComEd Br. at 88 & App. A, Schs. C-1, C-2.

**b. A&G Expenses --
Direct Assignment and Allocation**

ComEd, in refuting the arguments of Staff, IIEC, GC, and the ARES Coalition on functionalization of General and Intangible Plant in Section II.C.2, has thoroughly debunked those parties' arguments relating to the functionalization of A&G expenses. While the issues are distinct, Staff and those intervenors say nothing relevant here that has not been disproved there.

ComEd submitted overwhelming and largely uncontradicted evidence in support of its functionalization of A&G expenses, and the opposing arguments and proposals of Staff and intervenors were erroneous. ComEd Br. at 64-65. Staff once again relies on the Commission's ruling in Docket No. 99-0117. Staff Br. at 37, *et seq.* ComEd in Section II.C.2, above, has shown that Staff's reliance is unfounded, that the conclusion reached in that Docket simply does not justify Staff's position here, and that the Commission's reasoning in its Order in that Docket, in its Order on Rehearing, and in its Order in Docket No. 99-0013, all support ComEd because they all support using the most accurate functionalization that is feasible.

Staff also again relies on its assertions of inconsistencies in ComEd's methodology and testimony. Staff Br. at 38. As shown in Section II.C.2, no such inconsistencies exist, unless applying the same overall methodologies to the current facts and employing more refined allocators where direct assignment is not feasible are "inconsistencies". Staff's argument that

some FERC A&G Accounts have been allocated more to delivery services than was proposed in relation to the 1997 test year figures in Docket No. 99-0117 (Staff Br. at 39), does not even remotely show any “inconsistency” on ComEd’s part, much less any error. That ComEd in fact used the labor allocator for the approximately 25% of A&G expenses that are not amenable to direct assignment and for which that particular allocator bears an appropriate relationship to cost causation in this case, but did not for certain of these expenses in Docket No. 99-0117, shows no “inconsistency” or error, but, at most simply confirms” that ComEd used refined allocators where direct assignment was not feasible. Staff Br. at 39; Hill Sur., ComEd Ex. 45.0, pp. 15:305-16:326; Hill, Tr. 3428:4-14. That ComEd was able to do a better job of functionalization, either because of better data or more refined allocators, simply is not a rational reason to reject that functionalization.

Staff appears to assume that ComEd used direct assignment as to all of the costs that ComEd functionalized to jurisdictional delivery services. Staff Br. at 40. That also simply is not true. Again, ComEd used over 30 allocators for various A&G expenses that were not amenable to direct assignment. Hill Reb., ComEd Ex. 23.0 CR, pp. 15:305-16:326. Staff’s criticism of ComEd’s direct assignment of executive salaries (Staff Br. at 40) is flawed because it did not happen. ComEd used the above labor allocator to functionalize executive salaries. Hill Reb., ComEd Ex. 23.0 CR, pp. 15:305-16:326.

Staff’s remaining arguments (Staff Br. at 41-44) including for inflating the labor allocator by incorporating the fossil units ComEd sold in 1999, all reiterate erroneous claims Staff made regarding General and Intangible Plant. *See* Section II.C.2.

The intervenor arguments also lack any merit. IIEC, as noted earlier, combined its arguments relating to the functionalization of A&G expenses in Section II.C.2 of its initial brief.

GC simply reiterated its points relating to General and Intangible Plant. GC Br. at 47-48. The ARES Coalition offered nothing here, merely endorsing IIEC's position and asserting that ComEd failed to prove valid grounds for its functionalization. ARES Br. at 71. All of those arguments, as well as the ARES Coalition's spurious attacks on CBMS, are refuted in Section II.C.2. Assertions that ComEd has not proved its points are false. The evidence in the record makes clear that: ComEd's functionalization of A&G expenses is the only correct one.

**c. Proposed Known and Measurable
Changes to Test Year Expenses**

**(i) Expense Adjustments Related To Rate
Base Adjustments**

See Section II.D.3.c.i of ComEd's Initial Brief. ComEd Br. at 65-66.

(ii) "Levelization" Adjustments

GC claims that ComEd "made much" of Mr. Effron's use of different time periods for various adjustments he proposed, contending that there is no objective standard. GC Br. at 48. It is precisely Mr. Effron's use of a purely subjective standard, in which he picks and chooses different years whenever it suits him, that make Mr. Effron's adjustments so dangerous and groundless. Mr. Effron transparently chooses his normalization years on a single criterion -- maximizing proposed reductions to ComEd's jurisdictional revenue requirement. His result-oriented system selects years for "normalization" in which all the intervenors and Staff agree that ComEd spent too little on its distribution system. It makes no sense to set rates looking at the lowest expense years of the past, knowing full well that ComEd has instituted new maintenance programs that, as Mr. DeCamppli testified, "aren't cheap to invest in." Tr. 1445:21-25. It just cannot be credibly argued on this record that distribution O&M expenses are going down in the future. Moreover, GC's brief does not account for the seven flaws in Effron's analysis described in ComEd's Initial Brief (at 92-95).

(1) Tree Management Expense

ComEd voluntarily made a downward adjustment of \$513,000 to its jurisdictional test year tree management expenses, which were \$46,871,000, using a three year levelization period, 1998 to 2000, and no further downward adjustment or longer levelization period is appropriate. ComEd Br. at 67-68. Staff proposes an alternative downward adjustment of \$7,028,000, using an eight year average, premised on the fact that from October 1998 to May 2000 ComEd accelerated tree trimming in order to achieve a four year cycle (Staff Br. at 45-46), even though ComEd's 2001 budget is only approximately \$3,407,000 lower than ComEd's levelized figure of \$46,358,000. Voltz Dir., ComEd Ex. 5.0, p. 21:445-54; Voltz Sur., ComEd Ex. 46.0, p. 18:388-91. GC's alternative proposed downward adjustment is \$4,703,000 (erroneously not adjusted for inflation) using a six year levelization period. GC Br. at 49; ARES Br. at 72. Staff's and GC's alternatives are erroneous, for several reasons.

First, ComEd's three year period is appropriate given the specific activity and funding levels in those three years and going forward. *E.g.*, Voltz Reb., ComEd Ex. 24.0 CR, pp. 15:315-17, 16:323-35; Voltz, Tr. 1992:8-21. Second, ComEd's tree management activities and funding levels pre-1998 were insufficient for the four year cycle and resulting higher level of reliability that ComEd now is achieving, so levelizing using pre-1998 data is erroneous and, moreover, Staff and GC have chosen periods that plainly are biased to produce too low a result. Voltz Reb., ComEd Ex. 24.0 CR, pp. 14:282-15:300; Voltz Sur., ComEd Ex. 46.0, pp. 16:350-17:366; Effron, Tr. 2040:13-2043:16. Third, the evidence does not support the assumption that the accelerated tree trimming in fact incrementally increased costs. Accelerated tree trimming may decrease, not increase costs, Staff's witness made no independent determination that any such increase in fact occurred, and GC's witnesses also presented no such analysis. Voltz Reb., ComEd Ex. 24.0 CR, p. 16:318-25; Voltz Sur., ComEd Ex. 46.0,

pp. 16:367-17:384; Jones, Tr. 1704:8-1712:4. Cross-examination of Staff and GC witnesses confirmed the invalidity and mathematical bias of their proposals. Jones, Tr. 1704:8-1712:4; Effron, Tr. 2021:7-2022:5, 2038:5-2043:16; Schlissel, Tr. 2185:16-2187:14, 2187:20-2188:3. Their proposals are unsupported, arbitrary, biased, and results-driven.

(2) Storm Restoration Costs

ComEd voluntarily made a downward adjustment of \$2,946,000 to its jurisdictional test year variable storm damage restoration expenses, which were \$18,668,000, using a three year levelization period, 1998 to 2000, and no further downward adjustment or longer levelization period is appropriate. ComEd Br. at 68. Staff proposes an alternative downward adjustment of \$10,505,000, using a nine year average, premised on the results-driven theory that the 1998-2000 expense average was significantly higher than the average in prior years. Staff Br. at 46-49. GC proposes an alternative downward adjustment of \$5,771,000 (erroneously not adjusted for inflation), using a five year average, for that reason and because that period was used in Docket No. 99-0117. GC Br. at 49-50; ARES Br. at 72. Those proposals should be rejected. The evidence shows that in 1998, as Staff itself admits, ComEd significantly changed its handling of storm restoration, including implementing a policy of making temporary and permanent repairs, hugely decreasing storm outage durations; and, that in 1998 ComEd also materially changed its storm expense accounting, making pre-1998 data not comparable. Staff Br. at 46-49; Voltz Dir., ComEd Ex. 5.0, p. 21:433-42; Voltz Reb., ComEd Ex. 24.0 CR, pp. 17:349-19:392; Voltz Sur., ComEd Ex. 46.0, pp. 19:411-21:447, 21:462-22:469; Voltz, Tr. 1993:1-1997:9. Yet Staff unwilling to recognize the nature and significance of those facts. Sant Dir., Staff Ex. 3.0, pp. 15:295-16:314; Sant Reb., Staff Ex. 17.0 CR, pp. 4:74-9:168. Staff concedes that if ComEd is doing temporary repairs when it previously did not, then it “probably” cannot do that for free (Sant, Tr. 1739:20-22), but refuses to concede that the higher expense levels of 1998-2000 have

anything to do with ComEd's dramatic changes in its operations (or the changes in accounting) or that the pre-1998 data is not comparable. Staff insists that ComEd provide numerical quantification of the impact on expenses (other than the fact of the increased expenses themselves), even though the relation of the expenses to the changes is clear and such quantification is not possible. Voltz, Tr. 1993:1-1997:9. GC's testimony adds nothing, because it is based on the facts that 1998-2000 average expenses were higher plus the five year average used in Docket No. 99-0117. Effron Dir., GC Ex. 2.0, pp. 12:20-14:6. Finally, even assuming, incorrectly, that a longer levelization period would be appropriate, it would be 1998 to August 2001 -- not the periods proposed by Staff and GC -- resulting only in an additional downward adjustment of \$748,000. Voltz Reb., ComEd Ex. 24.0 CR, pp. 19:393-20:408; Voltz Sur., ComEd Ex. 46.0, pp. 19:401-10, 21:448-61. If that alternative were modified as raised by Staff to levelize both fixed and variable costs, then it would reduce, not increase, ComEd's proposed adjustment by \$600,000, but ComEd believes that consistency is better served by its alternative without that modification. Voltz Sur., ComEd Ex. 46.0, p. 21:448-61.

(3) Reserve for Levelized Variable Storm Damage Expenses

ComEd's Initial Brief showed that its proposed accounting reserve for variable storm expenses is in all parties' interests, is opposed only by Staff, and that Staff's objections are erroneous and in part rest on a misunderstanding of the proposal. ComEd Br. at 68-69 and n.†. That all remains true. Staff's assertion that stockholders obtain a unique benefit of recovering certain costs "risk free" (Staff Br. at 54) overlooks that any benefits to stockholders are part and parcel of the stabilization of earnings that benefits all parties (*id.*), ignores that under the proposal stockholders must fund the full reserve each year even if actual expenses are less (*e.g.*, Voltz Reb., ComEd Ex. 24.0 CR, pp. 23:485-24:493), and, in any event, does not change that

Staff is unable to identify anyone the proposal would harm and that allegedly uneven benefits are not a valid reason for rejecting the proposal, which is Pareto optimal. *E.g.*, Voltz Reb., ComEd Ex. 24.0 CR, pp. 20:420-21:427, 23:481-24:508; Sant, Tr. 1741:13-1745:15; Chalfant, Tr. 2553:1-13.

Staff's single issue ratemaking and test year argument (Staff Br. at 49-53) does not apply to a reconciliation mechanism such as proposed here. *Citizens Utility Bd. v. Illinois Commerce Comm'n.*, 166 Ill. 2d 111, 137, 651 N.E.2d 1089, 1102 (1995); Voltz Dir., ComEd Ex. 5.0, pp. 23:490-24:508; Voltz Reb., ComEd Ex. 24.0 CR, pp. 21:428-22:466; Voltz Sur., ComEd Ex. 46.0, pp. 22:471-87, 24:519-26:561. Staff's retroactive ratemaking argument (Staff Br. at 53) is a more serious concern, but ComEd respectfully submits that the two cases Staff cites are not directly on point to ComEd's storm reserve proposal, which sets up in advance a form of reconciliation measure for a uniquely variable cost, in which rates only are set prospectively in a ratemaking proceeding, and where Statement of Financial Accounting Standards No. 71 permits such a reserve Commission approval.[†] Voltz Dir., ComEd Ex. 5.0, pp. 24:513-25:524; Voltz Reb., ComEd Ex. 24.0 CR, pp. 23:481-24:508. Thus, unless the Commission believes that the proposal violates the retroactive ratemaking doctrine, it should be approved.

(4) Other

GC and Staff make certain recommendations for levelizing particular FERC accounts and salaries and wages, respectively, claiming that the 2000 test year is not representative of expenses. GC Br. at 50-56; Staff Br. at 54-57. All such proposals to levelize ComEd's O&M

[†] *Citizens Utilities Co. of Illinois v. Illinois Commerce Comm'n.*, 124 Ill. 2d 195, 529 N.E.2d 510 (1988), involves a downward adjustment to rate base ordered by the Commission outside a ratemaking proceeding based on past over-recovery of a particular cost. The case of *Business and Professional People for the Public Interest v. Illinois Commerce Comm'n.*, 136 Ill. 2d 192, 555 N.E.2d 693 (1989), involved a proposed settlement agreement in a ratemaking proceeding providing for retroactive refunds over each of five years outside of any ratemaking proceeding.

expenditures should be rejected. The Commission can be confident that ComEd's future O&M Expenses will be consistent with, if not higher than, expenditures from the 2000 test year. *See* Section II.D.4. In addition, with respect to compensation-related claims, ComEd has already made a \$4.7 million adjustment to salaries and wages as a result of certain activities and programs. Additional adjustments, such as those proposed by Staff or GC, would result in double-counting, and should be rejected. Voltz Sup. Reb., ComEd Ex. 39.0, pp. 2:41-3:57.

GC proposes levelizing FERC Accounts 580 and 590, and FERC Accounts 592, 593, 594 and 903; GC Br. 50-56. These should be rejected. *See, generally*, ComEd Br. at 92-95.

GC's witness Effron's proposed adjustment to Accounts 580 and 590 is unwarranted. The vast majority of the apparent variance in Accounts 580 and 590 between 1998 and 2000 resulted from accounting changes for incentive payments previously recorded in FERC Accounts 920 and 921, as well as refunctionalization from transmission to distribution. Voltz Reb., ComEd Ex. 24.0 CR, p. 11:213-18; Voltz Sup. Reb., ComEd Ex. 39.0, p. 6:122-32; Hill Reb., ComEd Ex. 23.0 CR, pp. 34:756-35:771. ComEd described in detail the various additional expenses that made up 85-90% of the expenses in both FERC Accounts. GC does not dispute these facts but, rather, claims that adding the year 2000 incentive compensation reflected in Account 580 to amounts in Accounts 920 and 921 represents an increase over the total incentive compensation recorded in previous years. GC Br. at 53. However, GC ignored the undisputed facts that the combined data from the three accounts reflect a \$5 million credit in Account 580 stemming from an over-accrual in the prior year (Voltz, Tr. 1999:11-2000:13, 2008:4-13), and that the data contained in the spreadsheet referred to by GC were not functionalized for purposes of this Docket. Voltz, Tr. 2008:14-21. Therefore, the data GC relies upon is of no value and its argument is wholly without support.

Mr. Effron's proposed adjustments to FERC Accounts 592, 593, 594 and 903 are similarly without merit. ComEd explained the reasons for increasing Account 592, and demonstrated that its expenses will continue at or above this level. Voltz, Sup. Reb., ComEd Ex. 39.0, p. 7:145-56; *see* Section II.D.4. Adjusting for inflation, 2000 figures represent an insignificant increase over expenses from previous years, almost a third of which occurred in FERC Accounts 593 and 594 as a result of refunctionalization. Voltz Sup. Reb., ComEd Ex. 39.0, pp. 7:145-8:171; Voltz Sur., ComEd Ex. 46.0, pp. 11:238-14:292. With respect to Account 903, GC conceded that an adjustment was required, as pointed out by ComEd. Hill Sup. Reb., ComEd Ex. 38.0 CR, pp. 9:203-11:230; Effron Reb., GC Ex. 5.1, p. 22.

Staff proposes an adjustment for ComEd's distribution salaries and wages, normalizing them at 1998 levels. Staff Br. at 55. After refunctionalization and inflation, the actual difference in ComEd's salaries and wages from 1998 to 2000 is a net \$13 million increase, which reflects substantial modifications to ComEd's distribution planning and maintenance efforts to maintain and improve reliability, and which will continue at or above current levels. Voltz Sup. Reb., ComEd Ex. 39.0, pp. 1:15-3:61; *see* Section II.D.4. Staff's proposed adjustment should therefore be rejected.

Discussion of the ARES Coalition's claims for adjustment resulting from purported "failures of the past" is contained in Section II.C.6.

**(iii) Salary and Wage Adjustment
for General Pay Increases**

See ComEd Br. at 71. ComEd agrees that, if any of Staff's erroneous salary and wage adjustments were to be adopted, then they should reflect to the extent applicable the wage increase due to the new labor agreements. Staff Br. at 57.

(iv) Adjustments for Post-Test Year “Merger Savings”

Certain parties propose that ComEd’s revenue requirement be adjusted for savings resulting from Unicom/PECO merger-related layoffs and the closing of certain bill payment centers. Staff’s and GC’s proposed reductions to test year expenses relating to employee reductions should be rejected as inappropriate and, in GC’s case, purely speculative and without evidentiary basis. ComEd Br. at 71-73. Staff’s proposed adjustment relating to bill payment centers is also meritless, as realized merger costs/savings have already been correctly reflected in the test year expenses. Hill Reb., ComEd Ex. 23.0 CR, p. 28:604-08.

If any adjustment is made, which it should not, the full impact of the costs that ComEd has incurred and will continue to incur must be considered, including severance compensation, payroll taxes, and other costs, which would necessitate an offset. ComEd Br. at 71-72; Helwig Reb., ComEd Ex. 19.0, p. 9:180-82; Hill Sur., ComEd Ex. 45.0, p. 40:854-64. Contrary to their claims, Staff has not cited a single case in which the Commission removed merger-related costs incurred in the test year over utility objection. Nor do these cases support Staff’s position that ratepayers should receive the benefit of speculative merger “savings” through an adjustment to test year expenses. In fact, in Docket 93-0252, the Commission specifically held that severance costs are recoverable, and must therefore be considered if any adjustments are made. No party has disagreed that, after taking into consideration severance compensation and related costs, ComEd will not achieve any cost savings until at least mid-2002, well beyond the test year. Therefore, any proposed adjustments are inappropriate.

d. Other Proposed Adjustments to Expenses

**(i) Exclusion of Incremental Expenses
Related to Unicom/PECO Merger**

ComEd voluntarily excluded 100% of its incremental jurisdictional operating expenses incurred in the test year related to the Unicom/PECO merger, an aggregated downward adjustment of \$34,515,000. ComEd Br. at 74. The GC's assertion that this large reduction is "illusory" is based on their erroneous assertions of alleged merger savings (GC Br. at 58-59), which ComEd refuted in Section II.D.3.c.iv, above.

(ii) Exclusion of Audit-Related Costs

ComEd's Initial Brief showed that it had voluntarily excluded all of its incremental jurisdictional operating expenses incurred in the test year related to Liberty and Vantage audits, a downward adjustment of \$2,098,000. ComEd Br. at 74. The ARES Coalition asserts that ComEd failed to exclude incremental costs of ComEd personnel participating in interviews for those reports. ARES Br. at 38. However, the evidence is uncontradicted that they did not result in any incremental costs. Juracek, Tr. 3396:15-3405:20.

(iii) Environmental Remediation Expenses

ComEd made a voluntary downward adjustment to its jurisdictional operating expenses for environmental remediation of \$16,850,000, showing that the GC's proposal for a levelizing adjustment is without merit and that the ARES Coalition's tardy assertion that these expenses are not costs of providing delivery services is irrelevant because these are proper corporate costs that should not be bypassed by any retail customer. ComEd Br. at 74-75. While the GC and the ARES Coalition renew those arguments (GC Br. at 59-60; ARES Br. at 74), they are refuted by the ComEd and Staff evidence and the Illinois Supreme Court case cited in ComEd's Initial Brief. *Accord* Hill Sur., ComEd Ex. 45.0, p. 22:466-72. As to the ARES Coalition's argument,

the Court explained that these expenses, like taxes, are legally mandated, utilities are entitled to recover such expenses from ratepayers, and they benefit ratepayers in that paying them allows the utility to remain in business and continue providing service. *Citizens Utility Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 120-124, 651 N.E.2d 1089, 1094-1097 (1995). Indeed, because these expenses, while not “distribution” expenses as such, must be paid in order for ComEd to continue providing service, they meet the definition of delivery services. 220 ILCS 5/16-102.

(iv) Advertising Costs

Staff continues to advocate the disallowance of 87% of jurisdictional advertising expenses. Staff Br. at 63-64. Staff changes its theory for this adjustment at every turn, which demonstrates the weakness of its position. First, Staff claimed that all but \$15,000 of these expenses were not allowable under Section 9-225 of the Act because the advertising was considered “goodwill or institutional.” Bowers Dir., Staff Ex. 4.0, p. 4:74-89. After ComEd challenged this conclusion, Staff relied on the entirely new and legally unsupported theory that, even if the advertising is allowable under Section 9-225, such advertising must be “directly related to the provision of delivery services” to be recoverable. Bowers Reb., Staff Ex. 18.0 CR, pp. 2:24-7:140. This argument is legally incorrect as identified in ComEd’s initial brief. ComEd Br. at 75-77. Staff now appears to abandon its “direct relationship test” argument. Staff Br. at 63-64. Staff apparently now argues that all of the advertising at issue (except for \$15,000 in costs) is goodwill or institutional and is therefore not recoverable under Section 9-225 of the Act.

The substance of the advertisements show that they fall squarely within the categories of ads allowable under the Act. Bowers Reb., Staff Ex. 18.0 CR, Att. A.. Staff now seeks to ignore its previous concession that it disallowed the advertising that was otherwise allowable under Section 225 only because the substance was, in Staff witness Bowers’ mind, unrelated to

delivery services. Bowers Dir., Staff Ex. 18.0 CR, pp. 2:40-3:47, 6:113-17. The Commission should reject Staff's ever changing and legally unsupportable position.

(v) Bank Commitment Fees

Staff claims that it disallowed 100% of these fees, \$902,000 because such fees “are a form of interest expense, which is considered a ‘below the line item.’” Staff Br. at 64. For ratemaking purposes, these expenses are appropriately moved back “above the line” and this treatment is consistent with prior Commission orders allowing recovery of these costs. Hill Reb., ComEd Ex. 23.0 CR, p. 14:298-99. Contrary to Staff's assertion, such expenses are separate and apart from interest expense and are not at all factored into the cost of capital analysis. Staff has asserted no legitimate reason for disallowing this expense, and no party refuted the past Commission practice of allowing these costs in revenue requirement.

(vi) Legal Expenses

Staff asserts for the first time in its Brief that it lacked sufficient information to evaluate the legal expenses. Staff Br. at 64-65. This argument is disingenuous. The document to which Staff refers in support of this argument, ComEd's A & G Study, which ultimately became ComEd Cross 29, was produced on June 7, 2001, six days after the petition in this matter was filed. ComEd's June 7 production also included all of the workpapers associated with the development and application of the allocators used to functionalize legal expenses. Staff served five rounds of data requests upon ComEd relating to this expense. ComEd responded to each request. During the five month discovery period, Staff never filed a motion to compel due to its belief that the information provided was insufficient. ComEd, in good faith, believed that it complied with all of Staff's discovery requests and Staff should not be allowed to now assert “lack of information” as a basis for disallowance. Legitimate delivery services expenses should not be disallowed because information sufficient to directly assign such costs simply does not

exist. Finally, Staff claims that the option it finds most preferable for allocation of jurisdictional legal expenses employs “the Company’s allocator.” Staff Br. at 65. This is simply wrong. ComEd Br. at 80-81.

(vii) Charitable Contributions & Memberships

Staff claims that the Commission should disallow \$110,000 in charitable contribution expenses solely because the recipients of the contributions were physically located outside of ComEd’s service territory. Staff Br. at 65-66. The relevant provision of the Act does not authorize a disallowance for this reason.

It shall be proper for the Commission to consider as an operating expense, for the purpose of determining whether a rate or other charge or classification is sufficient, donations made by a public utility for the public welfare or for charitable, scientific, religious or educational purposes, provided that such donations are reasonable in amount

220 ILCS 5/9-227 (emphasis added). Staff’s rationale is that ComEd failed to provide examples of any ratepayer receiving a benefit from such contributions. Staff Br. at 65. While such a showing is not necessary, the contributions at issue include support for engineering schools at the University of Illinois (Urbana, Illinois), the University of Wisconsin (Madison, Wisconsin) and Purdue University (West Lafayette, Indiana), which encourage curriculum in electrical and mechanical engineering, skills critical to ComEd. Hill Sur., ComEd. Ex. 45.0, p. 27:577-84, ComEd Ex. 45.3.

Staff asserts that it disallowed certain organizational dues because they were paid “other than to the Edison Electric Institute.” Staff Br. at 66. The dues were paid to the National Regulatory Research Institute, an affiliate of NARUC. Hill Sur., ComEd Ex. 45.0, ComEd Ex. 45.2. This expense was allowed in prior cases and should be allowed here. *Commonwealth Edison Co.*, Docket No. 99-0117 (August 26, 1999) pp. 22-40.

(viii) Special Projects

The ARES Coalition argues for the first time in its brief that 100% of the expenses associated with “Special Projects” be deducted from the revenue requirement because ComEd failed to prove that the “Jefferson Substation refurbishment, the Summer 2000 Readiness Program, and the data conversion project” represent recurring expenses. ARES Br. at 75. The ARES Coalition fails to explain why all of the costs should be disallowed where it only takes issue with three specific projects. The ARES Coalition’s only citation in support of its position is a blatant misrepresentation of the record. *Id.*

Q. Would you expect any costs relating to the Jefferson substation refurbishment to be recurring in that they will be incurred in coming years on a regular basis?

A. (Hill) I don’t have the responsibility in that area, so I wouldn’t know.

Q. Do you know—would you expect costs related to implementation of the 2000 summer readiness program to be a recurring cost and that they would be incurred in coming years on a regular basis?

A. My answer would be the same as the previous question.

Q. Would your answer also be the same with respect to extraordinary emergency restoration of power expenses?

A. It would.

Hill, Tr. 3455:17-56:11. This is hardly the “evidence” the ARES Coalition makes it out to be. ComEd met its burden of establishing the prudence of the expenses associated with special projects. Simply put, the ARES Coalition mischaracterizes the facts and the law on this point and its proposal, whatever it is, should be rejected.

(ix) Research and Development Costs

Staff asserts that it disallows these costs because “information provided by the Company indicated that the end result of the R & D would be a marketable product that has no delivery services characteristics.” Staff Br. at 67. Staff cites to no evidence in support of this contention. Whether a R & D effort results in a marketable product is irrelevant to the determination of

whether such expense is jurisdictional. Finally, if the Commission were to accept Staff's adjustment, it will disallow significant costs that are clearly jurisdictional. For example, the CHA project (expense of \$3,170,000, of which \$1,170,000 is jurisdictional) concerned the installation of back-up generators and other distribution and reliability enhancement equipment at various CHA facilities to offer outage protection and better reliability. Hill Reb., ComEd. Ex. 23.0 CR, p. 19:408-23 & Att. 3.

(x) Interest on Customer Deposits

Staff continues to assert that the Commission should increase ComEd's revenue requirement to reflect the fact that on December 6, 2000, the Commission reduced the interest rate that ComEd must pay on customer deposits. Staff Br. at 67-68. ComEd opposes this adjustment even though it favors ComEd because it does not meet the applicable legal standard. ComEd Br. at 85-86. The change, while temporarily known and measurable, is subject to future variability and therefore lacks the permanence of a legitimate test year adjustment.

(xi) Uncollectibles Expense

Only Staff and GC propose an adjustment. Staff Br. at 68; GC Br. at 60-61. ComEd anticipated the arguments of these parties and fully addressed same in ComEd's initial brief. ComEd Br. at 86. Uncollectible expense includes two components -- the actual test year expense and the expected incremental uncollectible expense resulting from an increase in delivery service rates. Staff agrees. Staff Br. at 68. However, Staff's proposal to substitute the estimated incremental percentage rate for the actual year expense is not based on any analysis of test year actual uncollectible expense. ComEd's actual test year uncollectible expense was based on a detailed review of the test year uncollectible account activity. Hill Dir., ComEd Ex. 4.0 CR, 16:334-43; Hill Sur., ComEd Ex. 45.0, p. 30:642-31:659. Finally, ComEd's estimate for the uncollectible expense impact from incremental revenue of 0.71% of revenue (Hill Dir., ComEd

Ex. 4.0 CR, Sch. A-2.1) is conservative when compared to the actual test year rate of 0.9% of revenue. Hill Dir., ComEd Ex. 4.0 CR, 16:339-42.

(xii) Taxes Other Than Income Taxes

The adjustment remaining at issue in this category is the inclusion in the revenue requirement of \$1,401,000 in State Use Tax. Staff proposes that the Commission disallow 100% of this expense, despite the fact that Staff recognizes it is a legitimate expense. Staff Br. at 69-70. Staff raises no new points in its brief and ComEd addressed its arguments. ComEd Br. at 87-88.

GC disagrees with Staff's position and acknowledges that ComEd's proposed use tax is appropriately included in the revenue requirement. GC Br. at 61-62. The only differences between ComEd's proposal and GC are: (a) GC's assertions that the use tax should be recovered over 3.25 years, and (b) the interest amount included in ComEd's proposal should be completely disallowed. GC's suggestion that ComEd recover this amount over time runs afoul of test year principles and should be rejected. Moreover, to disallow the interest expense, discourages ComEd from having an aggressive tax policy which would ultimately be detrimental to ratepayers. The jurisdictional Use Tax includes interest in the amount of \$505,420 (\$155,513 if recovered over 3.25 years). Effron Dir., GC Ex. 2.0 CR, Sch. DJE-4. GC argues that ratepayers should not be required to pay interest for late tax payment. GC Br. at 61. This argument is incorrect. As a business principle, ComEd only pays taxes which it believes are legitimately due under the tax laws. If ComEd employed a less aggressive tax policy, one would logically expect that its tax expense would be higher; therefore, ComEd's tax policy ultimately results in lower jurisdictional expenses. If the Commission disallows the interest component, it effectively punishes ComEd for having an aggressive tax policy.

(xiii) Incentive Compensation

ComEd's proposal for recovery of incentive compensation costs is reasonable and should be approved. In its initial revenue requirement, ComEd eliminated \$4.7 million of incentive compensation paid during the 2000 test year. Hill Dir., ComEd Ex. 4.0 CR, p. 26:554-59. This adjustment removed all incentive compensation that related to achievement of the Unicom/PECO merger. In ComEd's rebuttal testimony, ComEd agreed to an additional \$24,561,000 reduction in compensation proposed by Staff witness Bryan Sant to limit the issues in this case. Sant Reb., Staff Ex. 17.0 CR, Sch. 17.11; Hill Sur., ComEd Ex. 45.0, p. 38:815-21.

Although ComEd has already agreed to more than \$29 million in incentive compensation reductions, GC contends that an additional \$7,517,000 should be deducted based on Mr. Effron's proposed five-year normalization of incentive compensation expense. GC Br. at 62; Effron Dir., GC Ex. 2.0, GC Ex. 2.1, Sch. DJE-2.7. GC's contention is incorrect. Mr. Effron's proposed \$7,517,000 deduction represents the difference between his "normalized" incentive compensation level of \$38,977,000 and what he described as ComEd's "adjusted test year expense" of \$46,494,000. Effron Dir., GC Ex. 2.0, p. 25:14-16. But Mr. Effron prepared his normalization analysis before ComEd agreed to Mr. Sant's proposed disallowance of incentive compensation based on financial goals. The total incentive compensation recovery proposed by Mr. Sant and accepted by ComEd is \$33,211,000, not \$46,494,000. Sant Reb., Staff Ex. 17.0 CR, Sch. 17.11, p. 2. The \$33,211,000 incentive compensation amount to which ComEd has agreed is less than the \$38,977,000 five-year average incentive compensation amount that Mr. Effron calculates. Effron Dir., GC Ex. 2.0, GC Ex. 2.1, Sch. DJE-2.7. Therefore, acceptance of Mr. Effron's proposal would increase incentive compensation above the level proposed by Mr. Sant and accepted by ComEd. Given that ComEd has accepted a lower level of incentive

compensation than proposed by Mr. Effron, no further reduction is appropriate. Mr. Effron's proposed allocation methodology for incentive compensation is discussed in Section II.D.3.a.

4. Prudence of Expenses

While some detractors suggest that ComEd's efforts to improve reliability are short-lived, the evidence demonstrates that ComEd's 2000 test year O&M expenditures reflect its efforts to modify ComEd's distribution operational practices, resulting in continued efforts toward improving and maintaining reliability in the future. The record shows:

- ComEd has instituted prudent and effective management restructuring. Helwig Sur., ComEd Ex. 43.0, p. 8:162-64;
- ComEd's expenditures for the Feeder Inspection and Repair Program are scheduled to increase above the 2000 test year spending levels on an ongoing basis. Voltz Sup. Reb., ComEd Ex. 39.0 CR, p. 5:91-98;
- Maintenance programs designed to improve reliability will remain in place. Helwig Sur., ComEd Ex. 43.0, p. 8:165-66; DeCampli, Tr. 1379:12-22;
- ComEd's 2001 actuals are approximately the same as its 2000 spending levels, reflecting on-going spending at approximately the same level at the 2000 test year. ComEd Br. at 92;
- ComEd's 2001 and 2002 budgets demonstrate continued O&M spending levels. Helwig Reb., ComEd Ex. 19.0, pp. 3:45-55; 3:61-6:116, Helwig Sur., ComEd Ex. 43.0, ComEd Exs. 43.1 and 43.2; GC Cross Ex. 65, at A-2.
- ComEd will continue to incur O&M expenditures for reliability and flexibility of the distribution system in the Chicago area through ComEd's "Chicago Optimization Plan" will continue until at least 2005. Helwig Reb., ComEd Ex. 43.0, p. 5:109-12.

ComEd's expenditures are prudent. E.g., DeCampli Reb., ComEd Ex. 26.0 CR, p. 11:269-76.

E. Cost of Capital

ComEd, GC and Staff are the only parties who submitted testimony proposing a weighted average cost of capital ("WACC") for use in establishing ComEd's revenue requirement. Ebright Dir., ComEd Ex. 11.0, Sch. 11.1, p. 1; Walter Reb., COC Ex. 2.0, pp. 7:194-8:199; Freetly Sup. Reb., Staff Ex. 27.0, Sch. 27.1. Although ComEd's testimony supported a 9.95% WACC, in order to narrow the issues in this proceeding, ComEd is willing to accept the lower

8.99% WACC proposed in Ms. Freetly's testimony. Tr. 2945:19-46:3. GC also supports the 8.99% WACC proposed by Ms. Freetly. Tr. 2946:4-18. No other party submitted testimony calculating or supporting a different WACC.

The Commission should approve the 8.99% WACC proposed by Ms. Freetly because it is supported by substantial evidence in the record. Freetly Sup. Reb., Staff Ex. 27.0, pp. 1:14-2:20. ComEd's testimony supports a much higher WACC, and therefore substantiates that ComEd's WACC is at least as high as the 8.99% proposed by Ms. Freetly. Thone Dir., ComEd Ex. 8.0, p. 24:479-85; Ebright Dir., ComEd Ex. 11.0, Sch. 11.1, p. 1.

The Commission should make no findings concerning the POLR risks. GC suggests that the Commission address the issue because it "might arise at a later date in another case" (GC Br. at 15), but the Commission should decide only issues that are actually presented in this case. It should not enter advisory opinions on issues that might arise in future cases. The ARES Coalition contends that the Commission should reject any proposal to establish a higher cost of capital "due to the risks associated with" POLR (ARES Br. at 77-79), but no such proposal has been made in this case.[†] ComEd's testimony proposing a 9.95% WACC did not include an upward adjustment to reflect POLR risk. Thone Sur., ComEd Ex. 51.0 p. 3:46-49; Juracek Sur., ComEd Ex. 41.0, p. 31:718-33. Ms. Freetly's 8.99% WACC includes no upward POLR risk adjustment, and, in fact, she testified that "an upward adjustment ... is unwarranted." Freetly Reb., Staff Ex. 19.0 CR, p. 20:359-60. Given that there is no POLR risk issue before the Commission, there can be no decision on a POLR risk question that is not presented.

[†] The ARES Coalition also states that it supports the cost of capital proposed by IIEC (ARES Br. at 14, 59), but IIEC presented no cost of capital analysis in its testimony, (Stephens Dir., IIEC Ex. 1.0 CR; Chalfant Dir., IIEC Ex. 2.0 CR), and makes no cost of capital proposal in its brief. (IIEC Br. at 11)(containing no discussion of Cost of Capital Topic II.E).

Nonetheless, in order to correct the record and to dispel the misleading impression that the GC and the ARES Coalition briefs seek to leave concerning ComEd's POLR risk testimony, two points should be emphasized. First, ComEd's testimony in this case is consistent with that in the Genco transfer case, (Docket Nos. 00-0369/00-0394), stressing that restructuring has removed "the risks associated with owning and operating generation." Peltzman Dir., ComEd Ex. 9.0, p. 12:249-51. GC quotes testimony from the Genco transfer case indicating that the transfer "will not adversely affect either the cost of debt or the cost of equity." GC Br. at 18. ComEd has said nothing to the contrary in this case. Rather, ComEd carefully explained that restructuring removes some risks and adds others, and at this early stage in the process it is difficult to state how the risk profiles compare. Peltzman Dir., ComEd Ex 9.0, p. 12:249-54.

Second, GC and the ARES Coalition suggest that, if it were appropriate to consider POLR risks when determining cost of capital and if a higher cost of capital were being sought in this case on that basis, the Commission would have to deny the request because ComEd transferred its generating assets and abolished its fuel clause. GC Br. at 16-17; ARES Br. at 79. No such issue is before the Commission because no higher POLR-risk-based cost of capital is being requested in this case. But if it were, the proposition that GC and the ARES Coalition advance would have to be rejected. ComEd did not forfeit its right to a cost-based cost of capital when it exercised its statutory right to eliminate the fuel clause.

2. Cost of Debt

The ARES Coalition's request that the Commission allocate "the differing and appropriate debt costs between the supply business and the delivery business" (ARES Br. at 79), should be rejected because there is nothing to allocate. Ms. Freetly determined the actual cost of long-term debt on ComEd's books as of March 31, 2001, with appropriate adjustments described in her testimony and on Schedule 27.2. Freetly Sup. Reb., Staff Ex. 27.0, pp. 1:13-2:20, Sch.

27.2. The use of a March 31, 2001 reference date – after the transfer of ComEd’s generating assets to Genco – means that the only debt that Ms. Freetly considered is debt that supports the delivery services business. The 6.95% cost of debt calculated by Ms. Freetly is the cost of debt to ComEd as a delivery services company.

5. Overall Rate of Return

The Commission should approve the following overall rate of return proposed by Ms. Freetly (Sup. Reb., Staff Ex 27.0, Sch. 27.1):

<u>Class of Capital</u>	<u>Amount (000’s)</u>	<u>Percent of Total</u>	<u>Cost or Earnings</u>	
			<u>End of Year</u>	<u>Weighted</u>
Long Term Debt	\$6,965,641	57.14%	6.95%	3.97%
Preference/Preferred Stock	0	0.00%	0.00%	0.00%
Common Equity	<u>5,224,000</u>	<u>42.86%</u>	11.72%	<u>5.02%</u>
Total	<u>\$12,189,641</u>	<u>100.00%</u>		<u>8.99%</u>

F. Cost of Service and Rate Design

1. Cost of Service Study Issues

The law and the evidence in the record overwhelmingly support the use of marginal cost ratemaking and the rejection of the embedded and “across the board” approaches. ComEd Br. at 103-08. Marginal cost-based rates promote economic efficiency, assign costs in accordance with cost causation and send economically correct price signals. The DOE “strongly endorses” ComEd’s marginal cost approach, noting, among other things, that all four Ph.D. economists who testified in this proceeding “unequivocally” support it. DOE Br. at 2.

Despite clear law and persuasive evidence favoring the marginal cost approach, various parties argue that, because the Commission used embedded-cost based rates in the first delivery services rate cases, it should continue to do so in this case. IIEC Br. at 12; GC Br. at 62-63;

ARES Br. at 80-81; NEMA Br. at 5-6; Staff Br. at 86, 93. That is simply not so. As ComEd have often noted, the Commission's decision must be based on the evidence in the record. Prior Commission orders are neither precedent nor *res judicata*. The evidence in the record overwhelmingly supports the use of marginal cost-based rates. Moreover, the evidence is consistent with nearly two decades of Commission orders approving marginal cost ratemaking for ComEd's bundled services. ComEd Br. at 103.

The specific arguments raised by opponents of marginal cost-based rates were addressed in ComEd's initial brief and the testimony to which it refers. For example:

- Staff's claim that the greater efficiency of marginal cost ratemaking works only in the "artificial world of perfect competition," conflicts with decades of regulatory practice. Staff Br. at 87. There is simply no question that marginal costs are very much part of the real world of regulated utilities because they assist regulators in achieving outcomes that would be expected in a perfectly competitive world. Swan Reb., DOE Ex. 2.0 CR, pp. 2:33-3:46; *see also* DOE Br. at 3-4.
- Staff's claim that an embedded cost approach better reflects the principle that costs should be assigned to the party that causes them (Staff Br. at 89), conflicts with overwhelming evidence in the record showing that this is untrue. ComEd Br. at 103-04; Swan Reb., DOE Ex. 2.0 CR, p. 8:156-59. ("There is no basis in economic theory to use embedded costs to set rates....They bear no relationship to the cost that must be incurred by the utility in the future...")
- Staff's contention that embedded costs are "easier to determine" and do not involve "estimation errors associated with marginal costs," Staff Br. at 94, mistakenly assumes that ease of estimation is the relevant criterion when determining whether to base rates on marginal or embedded costs. As DOE explained, this proceeding aims to set rates for distribution service going forward, which means that forward-looking marginal costs are more "actual" (*i.e.*, more useful and more relevant) than backward-looking (embedded) distribution costs incurred over the past two to three decades. DOE Br. at 4-5; Swan Reb., DOE Ex. 2.0 CR, at pp. 10:210-11:246 ("Embedded costs are no more 'actual' than are marginal costs.").
- Staff is plainly wrong when it suggests that there is something illogical about basing rate design decisions on marginal costs when many customers use equipment that is already in place. Staff Br. at 89-91. As Dr. Swan has explained, "all customers who use the common distribution system are consuming on the margin and ... impose the same marginal cost on the system." Swan Reb., DOE Ex. 2.0 CR, p. 14:312-14. "Customers do not just exist. They demand and use electricity typically every minute of every day." And ComEd's marginal cost study "develops costs to provide service in response to this very real economic activity." Alongi-Kelly Reb., ComEd Ex. 32.0, p. 4:83-86. As a result, old and new

customers impose the same costs on the distribution system. DOE Br. at 6; Alongi-Kelly Reb., ComEd Ex 32.0, pp. 7:148-8:168. The contention that marginal cost principles apply only to new customers is fundamentally flawed. Alongi-Kelly Reb., ComEd Ex. 32.0, p. 7:142. (“the distinction between existing and new is artificial and inappropriate.”)

- Staff errs again when it suggests that ComEd’s advocacy of marginal cost-based rates is inconsistent with its indication that it would be willing to accept an allocation of 52.7% of overall delivery services costs to residential customers based on ComEd’s embedded cost study. Staff Br. at 93-94; ComEd Br. at 108. ComEd has consistently maintained that use of embedded cost-based rates is a flawed approach that the Commission should reject. ComEd’s willingness to reduce the overall portion of delivery services costs that are allocated to residential customers does not detract from its proposal to follow sound economics and design the rates of individual customer classes based on marginal costs. Juracek, Tr. 3278:17-3279:5.

a. Marginal Cost Study

ComEd correctly performed its marginal cost study, and appropriately used the EPMC method to develop its proposed delivery services rates. ComEd Br. at 106-07. Arguments that have been raised about the study are not valid, provide no basis for rejecting it, and certainly provide no basis for resorting to crude, “across the board” methodologies advocated by some parties. Specifically:

- GC’s suggestion that the study is unreliable because it was not prepared by economists (GC Br. at 64) is baseless. The marginal cost-based approach that underlies the study is supported by every Ph.D. economist who has testified in this case. The study itself was prepared by highly qualified ComEd managers who are most familiar with ComEd’s costs and rates and, therefore, are best able to apply the marginal cost principles overwhelmingly advocated by economists to the specific circumstances that affect the rates that the Commission must set.
- The contention that marginal costs exceed embedded costs by 25% (IIEC Br. at 12; Staff Br. at 86) has nothing to do with the validity of the study or the propriety of using marginal cost-based rates. Swan Reb., DOE Ex. 2.0 CR, pp. 6:116-7:132. The difference is addressed by the use of the EPMC method. Alongi-Kelly Dir., ComEd Ex. 13.0 CR, pp. 26:558-27:595. Dr. Swan confirms that ComEd’s proposed EPMC method is “precisely the reconciliation method that economic theory prescribes when not all prices for all components of service and for all customers can be set equal to the marginal costs of providing those services.” DOE Br. at 5; *see also* Swan Reb., DOE Ex. 2.0 CR, pp. 4:74-5:100.
- The argument that ComEd’s marginal cost study is simply a replacement cost study is incorrect for at least three reasons. First, the study “does not develop costs for ComEd facilities that actually exist in the field.” Alongi-Kelly Reb., ComEd Ex. 32.0, p. 2:33-34. It develops long-term incremental costs for facilities needed in response to an incremental increase in demand on the system at the time of peak load, and, in the case of customer-

related facilities, for the addition of a customer to the system. *Id.*, p. 2:34-41. Second, whatever concerns have been expressed about comparisons to “replacement costs” fail to recognize that “there must be a close correlation between the incremental cost of providing additional output (marginal cost) and the cost of new equipment to meet loads placed on the system (replacement costs).” Swan Reb., DOE Ex. 2.0 CR, p. 6:123-25. There is absolutely nothing wrong with use of “replacement costs” when they reflect the current, incremental costs of providing additional service. Third, to the extent that required or existing facilities differ from standard facilities, marginal costs in ComEd’s study are not based on replacement costs. Alongi-Kelly Reb., ComEd Ex. 32.0, pp. 2:23-3:52,10:209-14; Alongi-Kelly Sur., ComEd Ex. 50.0 CR, pp. 1:19-2:30; Alongi-Kelly, Tr. 1233:16-1234:18.

- GC’s complaint that the study “fails to recognize distinctive marginal costs of production...” (GC Br. at 65) is irrelevant because the study appropriately analyzes the marginal costs of delivery services, not of generation and energy costs. Alongi-Kelly Dir., ComEd Ex. 13.0 CR, p. 10:205-15.
- GC’s contention that ComEd’s marginal cost study “bears no relationship to the way in which distribution costs are incurred” because system capacity has not been reached (GC Br. at 65) is wrong because the study is based on long-term incremental costs. “In this long-term view, customers, through their economic activity of demanding and consuming electric power and energy, utilize ComEd’s facilities to their peak level.” Alongi-Kelly Reb., ComEd Ex. 32.0, p. 6:122-24.

Other claims about ComEd’s marginal cost study that have been raised by advocates of discredited, embedded cost ratemaking are addressed in detail in ComEd’s testimony. Alongi-Kelly Reb., ComEd Ex. 32.0, pp 2:22-15:314; Alongi-Kelly Sur., ComEd Ex. 50.0 CR, pp. 1:19-11:213; ComEd Br. at 106-107. In summary, ComEd’s study provides the Commission with the best possible basis for designing delivery services rates -- a basis that is consistent with economic theory and with the goals of efficiency, cost causation and accurate price signals that should guide the decision in this case

b. Embedded Cost Study

ComEd’s Initial Brief, pp. 107-08 demonstrated that, while marginal cost-based delivery services rates should be established in this proceeding, the alternative embedded cost study submitted by ComEd has been prepared appropriately. The objections to ComEd’s embedded cost study are unfounded. For example:

- IIEC’s claim that ComEd’s embedded cost methodology differs from the approach approved in Docket No. 99-0117 is incorrect. IIEC Br., at 13-17. The basic structure and functioning of the study are unchanged, and the improvements and other changes incorporated into the study provide no basis for rejecting it as IIEC advocates. ComEd Br. at 107-08; Heintz Tr. 2956:10-2957:7.
- IIEC notes that certain transmission subfunctions have been refunctionalized since the last case resulting in an increase in the demand related distribution costs allocated to these subfunctions, (IIEC Br. at 14), but there is nothing at all inappropriate about the refunctionalization or the resulting shift in costs. In fact, as ComEd noted in its brief at 107-08, the only methodological difference that Mr. Chalfant identified was the addition of the high voltage electric service station (“HVESS”) subfunction – an addition that increased the accuracy of cost assignment.
- IIEC’s observation that 90% of the new subfunction HV ESS is assigned to the over 10,000 kW class (IIEC Br., at 14) is perfectly consistent with the fact that over 90% of the load 69 kV and above is in the Over 10,000 kW class. Heintz Dir., ComEd Ex. 14.0 CR, ComEd Ex. 14.1, Sch. 2b, lines 7-8.
- IIEC’s contention that the HV ESS subfunction need not have been created in the embedded cost study because ComEd proposed a marginal-cost credit (IIEC Br. at 15) is not a valid criticism of Mr. Heintz or an accurate observation about the study. When Mr. Heintz prepared the embedded cost study, he did not know whether it would be used for purposes of designing the high voltage credit or not. Heintz, Tr. 2961:5-10. However the credit was designed, it was appropriate to include the high voltage subfunction because the purpose of defining the subfunctions of D and C is to employ to the maximum extent possible the cost detail provided by the USOA, and, ultimately, to allocate as accurately as possible the functionalized costs to the various customer classes on the basis of cost causation. Heintz Dir., ComEd Ex 14.0 CR pp. 10:177-11:196.
- IIEC comments generally on changes in the results of the current study and the one approved in Docket 99-0117, but IIEC itself recognizes that the studies are based on different data (Chalfant Tr. 2541:13-42:21) which understandably affects their outcomes. The suggestion that changes should have fallen within a 5% bandwidth has no basis whatsoever. The fact that the class-by-class changes in revenue requirement between the earlier study and the current one do not meet IIEC’s arbitrary standard is an irrelevant as well as arbitrary “apples and oranges” comparison. Heintz Reb., ComEd Ex. 33.0, p 12:278-82.
- IIEC incorrectly insinuates that inaccuracies in ComEd’s embedded cost study are indicated by the use of generic ratios in bundled cost studies and the direct assignment approach in the delivery services study. IIEC Br. at 7. The evidence clearly demonstrates that “in the context of ComEd’s provision of D+C through its delivery service tariffs, it is imperative that all costs be functionalized as accurately as possible... to the greatest extent possible by direct assignment according to the results of detailed studies.” Heintz Dir., ComEd Ex. 14.0 CR, p. 18:335-40.
- GC’s contention that the more appropriate allocator for use in the study is the 4-coincident peak (4-CP) method proposed by Mr. Bodmer is not supported by the evidence. GC Br. at 72. Mr. Born testified that the 4 CP method of cost allocation is not a realistic representation

of how ComEd plans capacity additions to the distribution system. “Using an average of the four highest monthly peaks to determine capacity requirements would result in substantial overloads of most system facilities and unsatisfactory system operating performance.” Born Reb., ComEd Ex. 37.0, p. 7:121-25; See also Heintz. Tr. 3008:4-14; Heintz Sur., ComEd Ex. 57.0, p 1:18-21.

- GC’s contention that ComEd’s *marginal* cost study uses a coincident peak rather than a non-coincident peak method for 90% of costs is not a criticism of ComEd’s *embedded* cost study. GC Br., at 74. Moreover, Mr. Bodmer, who suggested the 90% figure (Bodmer Reb., GC Ex. 4.0, p. 39:828-31) also suggested a 62% figure (Bodmer Dir., GC Ex. 1.0, p 61:1204-06). Mr. Bodmer admitted that he was in error and corrected his testimony, changing the figure to 59%. Bodmer, Tr. 1827:1-9.
- GC’s proposed direct assignments of costs (GC Br. at 75-79) are unsupported and provide no basis for altering traditional allocations of customer-related expenses. Heintz Sur., ComEd Ex. 57.0, p. 2:25-27. Moreover, a review of Account 903 shows that over 75% of the costs in that account are based on individual customers and allocations should be and are made on a per customer basis. Heintz, Tr. 3015:14-16:12.

As with ComEd’s marginal cost study, the criticisms of ComEd’s embedded cost study are unfounded and should be rejected. The evidence establishes that the study was prepared properly and, although it is not and should not be the basis for ComEd’s delivery services rate design, it reflects expert judgment and correct resolution of all of the methodological issues raised by the parties who have commented concerning it.

2. Interclass Revenue Allocation

TrizecHahn and the IIEC propose an “across the board” allocation for all nonresidential customer classes. TrizecHahn Br. at 8, 14; IIEC Br. at 17-18. Such “across the board” proposals are clearly results-driven, a transparent attempt to gain subsidies for particular commercial and industrial customers at the expense of others, and should be rejected.

An “across the board” approach should be employed only where an accurate cost of service study does not exist. See Chalfant, Tr. 2534:21-2535:6. In this proceeding, ComEd has presented not one but two properly performed cost of service studies -- a marginal study, which is the superior ratemaking model, as well as an embedded study, which ComEd does not propose, but is willing to accept, for the highest level allocation for residential customers as a

whole and for nonresidential customers as a whole. *See* ComEd Br. at 108. The appropriateness of ComEd’s cost of service studies is discussed in Sections II.F.1.a and b.

The law properly recognizes that costs should be borne by the cost-causers. 220 ILCS 5/16-108(c). Allocating ComEd’s revenue requirement for nonresidential customers “across the board” sends improper price signals, discouraging economic efficiency by improperly allocating costs. *Makholm Sur.*, ComEd Ex. 55.0 CR, pp. 16:388-17:408; *Juracek Sur.*, ComEd Ex. 41.0 CR, p. 29:677-85. The particular cases from the 1970’s cited by the IIEC as precedent for “across the board” ratemaking did not use an absolute across-the-board approach and, in contrast to Intervenor proposals, were found to accurately reflect the utility operational trends as shown in the cost study presented. In addition, since the time of those cases, Section 16-108 of the Public Utilities Act has become effective, specifically requiring that delivery services rates be cost based. 220 ILCS 5/16-108(c). ComEd’s proposed allocation method using the EPMC is appropriate, and in no event should the Commission use an across-the-board allocation. DOE Br. at 9-10.

G. Rate Design

1. RCDS Rate Design

a. Demand Ratchet

ComEd proposes an annual demand ratchet for all demand metered non-residential delivery services customers. However, even were the Commission to reject this general rate design, it is imperative that an annual ratchet be used for stand-by and generation customers. *Clair-Crumrine Reb.*, ComEd Ex. 31.0 CR, p. 20:442-52. If not, delivery services customers as a whole will be unfairly forced to bear costs of facilities used only by stand-by customers who, in effect, will have free or nearly-free service. *Clair-Crumrine Dir.*, ComEd Ex. 12.0 CR,

p. 17:388-92. Moreover, if the Commission is at all uncertain about the use of a ratchet in delivery rates, use of a limited ratchet for this group is an ideal test or pilot prior to 2005.

(i) General Service Ratchet

The reason to use an annual demand ratchet for delivery services rates is simple, powerful, and undeniable. The cost of the distribution facilities serving a customer does not vary with changes in the customer's monthly energy use, or with short-term monthly fluctuations in its demand. The cost of its distribution facilities is determined by the facilities installed, which is in turn determined by the load that customer has historically demonstrated. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, pp. 14:323-19:430; *see also* ComEd Br. at 109-10; DOE Br. at 10-11. It cannot be seriously denied that, of the practical billing determinants available, the annual demand best reflects the actual cost of the delivery facilities installed. Clair-Crumrine, ComEd Ex. 112.0 CR, p. 15:330-345. The DOE, ComEd's largest active customer, agrees and supports this rate design. DOE Br. at 10-11. Several other parties, however, do not. Some attempt to deny the undeniable fact that distribution costs are more closely tied to ratcheted demand than any other practical measure. Some offer other "policy" arguments. Not one of the criticisms of the annual ratchet is valid.

The ARES Coalition, GC, and to a lesser extent, Staff claim that annual demand is not a true measure of distribution facility use. ARES Br. at 82; GC Br. at 81; Staff Br. at 96-97. As noted above, the evidence simply contradicts their assertion. Although not every new customer peak requires new facilities, every new annual customer peak does mean that a greater share of the existing local distribution equipment was, in fact, needed to serve that customer. There is no just reason that the "high peak" customer should be subsidized by other customers who have not set new, higher peaks. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, pp. 18:413-19:427; Swan Dir.,

DOE Ex. 1.0 CR, at 19:391-93.[†] Moreover, while it is true that annual demand does not correlate *perfectly* with distribution facilities costs -- local or regional peaks can also contribute - - the effect of customer peaks predominates. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, p. 15:330-45. But, more importantly, arguing over perfection is a red herring. Some billing determinant must be selected. And, it cannot be denied that using each customer's annual demand is the best measure of that customer's contribution to distribution facilities cost. An annual ratchet fairly balances the need to "get the price" right with concerns of customers having legitimately varying use. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, pp. 18:413-19:427.

BOMA, TrizecHahn, and the ARES Coalition assert that there should not be an annual ratchet for delivery services customers because there is none in bundled rates.[†] This argument is illogical. Bundled rates are designed to recover different costs (especially generation costs), having different drivers, than delivery rates. *E.g.*, Haynes, Tr. 1033:17-1034:3. The annual demand ratchet is the correct driver for delivery costs and will minimize cross subsidies for delivery customers. "Delaying action to address these cross subsidies [until bundled rates can be

[†] GC quotes out of context, and without citation, a Nobel laureate speculating on why utilities propose demand ratchets. GC Br. at 82. This is ironic given its dogged support of embedded cost ratemaking methodologies that no credible economist, Nobel laureate or not, supports. Lazare, Tr. 2790:15-2791:12. In any event, the speculation that ComEd's ratchet is intended to increase its revenues is false. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, p. 14:318-22.

GC also goes so far as to argue that customer demand can be met by running existing equipment at emergency ratings. GC Br. at 82. This is irresponsible, especially for a party promoting prudence. ComEd does not *plan* to meet customer load by running equipment this way. And, rate design should discourage, not be based on, using emergency capacity for normal load. GC's argument is also inconsistent with its claim that use of emergency ratings increases costs. GC Br. at 35.

[†] At the same time, the ARES Coalition argues for a more complex demand ratchet with seasonal factors and declining six-month weighted averages. The evidence does not show that this complex design better reflects ComEd's costs, and it is difficult to understand and cannot be billed. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 14:304-10. It should be rejected.

changed] is unfair to those customers who are paying them.” Clair-Crumrine Sur., ComEd Ex. 49.0 CR, p. 6:126-27.

TrizecHahn and BOMA also claim that eliminating the subsidies caused by non-ratcheted demand is somehow anti-competitive. TrizecHahn Br. at 15; BOMA Br. at 10-11. This is nonsense. Eliminating the subsidy currently given poor load factor customers will benefit the customers who have paid for the subsidy in the past, while giving correct price signals to all customers considering switching. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 14:318-15:334. TrizecHahn’s special reference to winter-peaking Rider 25 space heating customers misses the point. TrizecHahn Br. at 16-17. Even space heating delivery customers should pay a rate based on the facilities that they use, regardless of how bundled rates would recover their energy costs. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 14:311-15:334. Nor is there any truth to the related argument that an annual ratchet unjustly harms customers with energy management systems. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 13:289-303.

Finally, Staff and TrizecHahn oppose use of annual demands because the Commission did not approve an annual ratchet in ComEd’s last case. Staff Br. at 98-99; TrizecHahn Br. at 15. That is no reason to reject it now. The Commission must base its decision in this case on the evidence in this case and on the specific proposal made here. Indeed, Staff recognizes this fact and freely argues that the Commission should change its position on other topics (e.g., transmission service issues). ComEd has demonstrated that the ratchet proposed in this case is fair to customers and promotes efficiency. It should be adopted.

(ii) Special Ratchet for Standby Customers

The case for the use of a demand ratchet for stand-by and generator customers is even stronger. These customers undeniably use significant distribution facilities. Significant facilities are required, at a minimum, to back up the generation. Clair-Crumrine Dir., ComEd Ex. 12.0

CR, pp. 17:388-18:412. Yet, absent an annual ratchet, they will pay no facilities charge for this use unless the generating equipment happens to fail that month. *Id.* This is unjust and unfair to other customers. Indeed, no one can seriously claim that parties whose stand-by needs require the installation and maintenance of facilities should pay for them, at best, only sporadically. *Id.*; Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 16:359-17:388.

IIEC's argument to the contrary is grounded on the premise that stand-by and generation customers can be compared to non-standby customers; that is the basis of their argument that treating these customers differently is "discriminatory." The facts refute them, however. Standby and generation customers have very different load characteristics. Their energy use tends to be so sporadic and slight that unratcheted delivery rates would not come close to recovering their cost of service. Clair-Crumrine Sur., ComEd Ex. 49.0 CR, pp. 6:131-7:155.[†] There is nothing discriminatory about treating differently situated types of customers differently, especially where differences in rate design are economically justified. *E.g., Cerro Copper Prods. v. Illinois Commerce Comm'n*, 83 Ill. 2d 364, 372-73, 415 N.E.2d 345, 349 (1980). In this case it would be unfair not to treat them differently. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 15:336-17:388. Indeed, IIEC witness Stephens' own suggestion to use contract demand reinforced this point, "implicitly recogniz[ing] that customers who self-generate have facilities in place that are not appropriately paid for by the benefiting customer when charges are based on monthly demands." Clair-Crumrine Sur., ComEd Ex. 49.0 CR, pp. 7:158-60; 7:156-8:71.

NEMA's argument to the contrary is nothing but a naked request for subsidies for distributed generators. NEMA Br. at 8-9. The Act requires delivery services rates to be cost-

[†] IIEC's discussion of Rate 18 does not support its position. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 17:389-19:441. The design of that rate is influenced by its need to recover commodity costs. Clair-Crumrine Sur., ComEd Ex. 49.0 CR, p. 7:147-55.

based (220 ILCS 5/16-108(c)); any provision for subsidies to generators is conspicuously absent. Moreover, the evidence clearly shows that generators of all types, including specifically distributed generators, face just and reasonable rates and operating conditions in ComEd's territory, and have been able to participate in the market. Naumann Sur., ComEd Ex. 58.0, pp. 16:346-17:367; Naumann Reb., ComEd Ex. 35.0, pp. 23:501-24:525. Indeed, the evidence shows that a ratchet promotes efficient distributed generation by increasing the economic value of peak-shaving. Clair-Crumrine Dir., ComEx. Ex. 12.0 CR, p. 18:407-12. NEMA's witness was largely ignorant of these facts.

b. Definition of Billing Demand in Rate RCDS

The ARES Coalition erroneously implies that ComEd's proposed tariffs constitute a "change [to] the definition of billing demand for its DST customers". ARES Br. at 86. That is simply not the case. For all but a small percentage of RCDS customers, monthly billing demand is derived from the single highest 30-minute demand, which is identical to bundled service billing demand. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 33:759-66, 34:770-72.

As ComEd has explained, for the small percentage of customers taking service under Rider 6L - Large General Service ("Rider 6L"), a monthly billing demand obtained by averaging the three highest 30-minutes demands, rather than the single highest 30-minute demand, is appropriate. A billing demand definition that uses an average of the three highest 30-minute demands is necessarily lower than the single highest peak. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 34:767-81. It is therefore appropriate to use a single monthly peak for smaller non-residential customers for whom distribution is important to ensure that the charges accurately reflect the costs imposed on ComEd's distribution system. In contrast, the vast majority of costs to serve Rider 6L customers relate to generation, not distribution. Therefore, it is appropriate to

base the billing demand for these customers on the system peak, by using an average of the three highest 30-minute demands.

The ARES' Coalition's suggestion that, as an alternative, billing demand be determined twice a year using a convoluted series of options is incompatible with ComEd's billing system, would not permit ComEd to develop charges to recover its revenue requirement in this case, and should be rejected. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 34:782-89; Clair-Crumrine Sur., ComEd Ex. 49.0 CR, p. 14:308-17. The ARES' Coalition's claim that the use of ComEd's billing determinants results in ComEd's over-recovery is erroneous, if not disingenuous. ARES Coalition Br. at 85. The individual customer charge is determined by dividing ComEd's total revenue requirement by the billing determinant applicable to the particular class. Though the unit charge may therefore differ between classes, ComEd's revenue requirement remains the same. ComEd's billing determinants do not result in over-collection but, rather, permit ComEd to recover its distribution costs from the true cost-causers.

c. Impact on CTCs

BOMA contends that ComEd's rate design proposals will result in rate shock because increases in rates within a class attributable to changes in rate design are less likely to be offset by reductions in CTCs than increases attributable to revenue requirement changes. BOMA Br. at 11-14. BOMA's point, even were it correct, would not justify perpetuation of the cross subsidies that ComEd's proposals are designed to eliminate. For example, DOE demonstrates that any analysis of rate design changes on the opportunities for savings through participation in the open access system must consider all parties. As Dr. Swan explained:

the overcharge to high voltage customers is currently making it more difficult for them to save money by purchasing power from ComEd's competitors. Eliminating the subsidy will have the opposite effect. It will, other things constant, encourage more high voltage customers to take delivery service from ComEd and buy their power from alternative suppliers.

Swan Reb., DOE Ex. 2.0 CR, p. 30:684-88. If some rate increases resulting from elimination of cross subsidies are not absorbed fully by reductions in CTCs, the beneficial impact on customers who have been overcharged nonetheless warrants the changes.

The ARES Coalition contends that, even if ComEd receives no additional revenue as a result of its proposals, the Commission should be concerned about the portion of ComEd's revenue that is attributable to CTCs as compared with the portion that is attributable to the delivery services revenue requirement. ARES Br. at 87-90. Nothing in the Act supports this contention. ComEd is entitled to cost-based delivery service rates and that is what the Commission must approve. Any effect on CTCs is merely a byproduct of setting rates in accordance with the Act's requirements. The portion of the revenue from customers that is attributable to CTCs has nothing to do with the Commission's duty to establish cost-based rates.

d. Generation Facilities Under Rate RCDS

(i) Proposals for Production Credit

(ii) Proposals for Production Adder

Midwest argues that IPPs should be entirely exempt from distribution facilities charges at interconnection points where they deliver energy to the grid, regardless of whether the IPP actually use distribution facilities. Midwest Br. at 16-17, 18n.15. Midwest's argument is grounded on three erroneous factual premises.

First, Midwest says that "Where IPPs take station service over connections intended to move power out of their generating stations, IPPs impose no distribution facilities costs on ComEd." Midwest Br. at 8. Midwest is simply wrong. All of its interconnections use distribution facilities in varying amounts. ComEd Br. at 113-14. Some use a great deal of distribution equipment, especially those at lower voltages used for Midwest's many peaker

plants.[†] *Id.* at 114. ComEd’s functionalization of assets is proper, which Midwest does not dispute. *Id.* at 113.

Second, Midwest says that when its interconnections use distribution facilities sized to the generating unit’s output capacity, its use of distribution facilities for generally lower-demand retail station service can impose no additional or unrecovered costs on ComEd. *E.g.*, Midwest Br. at 2-3. This is also incorrect, for several reasons.

- Additional facilities or capacity may in fact be required, regardless of the comparative magnitude of the flows. ComEd Br. at 113-114; McLeod, Tr. 2341:4-2346:12. Indeed, some classes of additional distribution equipment (*e.g.*, retail revenue grade metering and telemetry) almost always are. Naumann Reb., ComEd Ex. 35.0, p. 8:177-81.[†] No matter how large the generator, those distribution costs are incremental.
- Midwest, or any IPP, uses *all* of the installed distribution facilities to take retail service to its plants, not just the additional, or “incremental,” facilities *only* used only for the inflow. Midwest, like every other retail customer, should pay its fair share of all of the distribution facilities that it uses. ComEd Br. at 112-14. That includes a share of the costs of the capital, operating, and maintenance costs of all of the distribution facilities that carry the inflow, allocated in accordance with the cost of service study. It matters not whether some of those facilities also carry outflow.
- Midwest misunderstands the distribution facilities charge. Apart from recovering the cost of specific types of facilities, this charge recovers substantial portions of the General and Intangible Plant and A&G expense. Alongi-Kelly Dir., ComEd Ex. 13.0 CR, ComEd Ex. 13.1. Midwest clearly uses a number of retail distribution services in connection with its consumption of power and energy, and Midwest should bear its share of the costs of those services, including a share of the common and overhead costs. If the facilities charge is arbitrarily set to zero, Midwest will dodge any share of those properly-allocated costs.

[†] ComEd does not agree that Midwest or IPPs as a general matter have only “minor or incidental” distribution facilities at high-voltage interconnections. Midwest Br. at 3, 5. Some do; some do not. The fact that the interconnection is high-voltage or sized for output does not mean that there are no distribution facilities. Naumann Reb., ComEd Ex. 35.0, pp. 8:172-9:185, 16:339-55; Born Reb., ComEd Ex. 37.0, p. 8:138-56; Born Sur., ComEd Ex. 59.0, p. 4:66-72.

[†] Portions of Midwest’s brief make claims about complex engineering issues concerning system planning and design, congestion, power flows, and the like, with which ComEd strongly disagrees, but which cannot be discussed in detail in a brief of this length. The evidence supports ComEd. *See* Naumann Reb., ComEd Ex. 35.0, pp. 13:287-14:309, 17:363-82; Born Reb., ComEd Ex. 37.0, p. 8:137-56; McLeod, Tr. 2318:15-2329:20, 2341:4-2346:12. However, resolution of these details is not required for decision of this case.

- Midwest misunderstands ComEd's cost of service study (which it supports) and the proper role of marginal costs. ComEd does not argue that users should pay a rate equal to marginal cost. ComEd argues, correctly, that marginal costs should be used to allocate the full embedded revenue requirement. ComEd Br. at 108; Alongi-Kelly Dir., ComEd Ex. 13.0 CR, ComEd Ex. 13.1. The fact that a given facility had to be built for another user, or for another use, should not exempt Midwest from paying a share of its cost any more than any retail customer hooking up to an existing, substantially loaded line could claim that they should be exempt from facilities charges because they require no additional facilities.
- Midwest misunderstands ComEd's recovery of costs for the distribution facilities serving its plants. ComEd is not recovering the full cost of distribution facilities that carry outflow in its transmission rates. In fact, ComEd has not included any distribution facilities in its base transmission rate. ComEd Br. at 130. Therefore, unless ComEd can recover distribution charges for these facilities in the delivery rate, the unrecovered costs will be borne by other customers. Under these circumstances, Midwest's witnesses admit ComEd's proposal is proper. Schink, Tr. 2295:13-2296:6; McLeod, Tr. 2307:4-2308:5.

In short, entirely exempting IPPs from distribution facilities charges at their "output" interconnections, as Midwest proposes, will result in a substantial, unjustified cross-subsidy. *See* ComEd Br. at 114. This subsidy is unnecessary and improper under both established ratemaking principles and the General Assembly's direction that "Charges for delivery services shall be cost based, and shall allow the electric utility to recover the costs of providing delivery services through its charges to its delivery service customers that use the facilities and services associated with such costs" 220 ILCS 5/16-108(c). *See also* Naumann Sur., ComEd Ex. 58.0, p. 11:228-37; Strobel Reb., ComEd, Ex. 18.0, p. 5:96-104. Indeed, Midwest itself emphasizes the importance of charging cost-causers and the impropriety of subsidies. *E.g.*, Midwest Br. at 3, 7.

Third, Midwest argues that it is "anti-competitive" for Midwest to pay the same facilities charge as every other customer, including other IPPs with newer generating facilities, because ComEd did not optimally wire the fossil stations' internal electric supply systems prior to selling the plants to Midwest. Midwest Br. at 15. Midwest seriously errs. Midwest is offered the same delivery rate as other IPP customers. The notion that Midwest is discriminated against by ComEd's rates is false. Any difference in the cost of delivered energy is a function of the

internal wiring of Midwest's plant, which Midwest is free to change, not of ComEd's rates. It is true that Midwest would have to pay for that rewiring, but so would any other customer who considers rewiring to gain energy efficiency. ComEd does not offer lower rates to any other customer who happens to have less efficient customer-owned wiring. There is nothing anti-competitive about expecting Midwest to pay the actual costs of the facilities that it uses. Naumann Sur., ComEd Ex. 58.0, p. 11:228-37.

Indeed, it is Midwest's position that is anti-competitive. Midwest was fully aware of how the fossil stations was wired before it purchased them, and surely took this fact into account when it valued those assets. Naumann Sur., ComEd Ex. 58.0, pp. 4:67-84, 10:208-17. But, by asking for ComEd to artificially eliminate the "down-side" of that wiring, Midwest seeks an unfair advantage over other generators who put the money into building "behind the meter" wiring in the first place. *Id.* at 4:85-5:101.

Nonetheless, as Midwest notes, ComEd and Midwest agree on much. *See* ComEd Br. at 114-16. Subject to the imprecisions inherent in any rate design, we agree that "Midwest should not pay for distribution facilities that it does not use." Midwest Br. at 4. But neither should Midwest avoid paying for facilities that it does use. And, neither should other customers pay for facilities used only by Midwest. IPPs should, as a group, pay for the distribution facilities they use -- no more, but no less. That is what ComEd's proposal accomplishes. Defining IPPs as having no standard facilities, and recovering the cost of the exact distribution facilities used by the IPPs through a Rider 6/7 mechanism, will properly place on IPPs the cost of these facilities -- calculated in the same, Commission-approved and non-discriminatory manner as charges for non-standard distribution facilities for every other customer. ComEd Br. at 115-16.

Finally, Midwest's objections to ComEd's proposal to address the needs of IPPs are meritless. Midwest Br. at 20-24. Midwest's suggestion that it pay only the marginal cost of the distribution facilities leaves others to carry its share of the common costs, as noted above. And, Midwest's suggestion that the cost be based on the theoretical manner in which Midwest would like to wire the plants ignores facilities that are in place, and used and useful. That, in hindsight, Midwest would have wished the system to be built differently is no reason to allow Midwest to avoid paying the costs of the facilities that it uses. Nor, again, is this anti-competitive. Naumann Reb., ComEd Ex. 35.0, pp. 18:401-20:430; Naumann Sur., ComEd Ex. 58.0, pp. 10:208-11:227. Midwest bought the plants, wiring and all, with its eyes wide open. It would be anti-competitive to allow Midwest alone to alter its deal and shift costs that were part of the bargain to others.[†] Naumann Sur., ComEd Ex. 58.0, pp. 4:67-5:101.

2. Rider HVDS

Seven parties address ComEd's proposed HVDS credit. DOE and Midwest support the proposal. Staff and IIEC agree with it in principle, but propose modifications. And BOMA, TrizecHahn, and the ARES Coalition oppose it.

Most of the arguments raised in opposition to Rider HVDS or in support of modifications to it were addressed in ComEd's initial brief. ComEd Br. at 116-21. It showed that the HVDS credit should be approved because it dramatically improves the allocation of costs by eliminating cross subsidies flowing from high voltage customers to other customers. The strongest opposition comes from the beneficiaries of subsidies, who seek to perpetuate them.

[†] For a discussion of the principle of *caveat emptor*, addressed in Midwest Br. at 19, see Naumann Sur., ComEd Ex. 58.0, p. 4:67-84 and Naumann, Tr. 1667:3-1670:1.

a. Eligibility

IIEC agrees that ComEd's Rider HVDS "very appropriately" recognizes and addresses the lower cost of serving customers at 69,000 volts and above, IIEC Br. at 24, but argues that a smaller HVDS credit should also be provided to customers served at 34,500 volts. *Id.* at 23-24. The DOE correctly notes that "[d]ifferent rate treatment must be reserved to account for significant differences in cost." DOE Br. at 14. The evidence simply does not warrant expansion of Rider HVDS to include customers served at 34,500 volts. ComEd Br. at 117.

Although Staff witness Michael Luth previously advocated establishment of a new high voltage rate class, Staff's brief now supports ComEd's approach of eliminating cross subsidization through an HVDS credit. Staff's Br. at 101. The ARES Coalition continues to argue for "a full set of rates based upon voltage levels" (ARES Br. at 91-92), and their argument should be rejected for the reasons discussed in ComEd's Initial Brief (at 123-24). Finally, the Commission should give no weight to TrezecHahn's baseless argument that the HVDS credit should be rejected because Sears Tower, which is not served at 69,000 volts or above (Clair-Crumrine, Tr. 1098:22-1100:20) is ineligible for it. TrizecHahn Br. at 20.

b. Calculation of Credit

BOMA and TrizecHahn contend that ComEd's calculation of the amount of the credit overstates the difference in costs between serving customers over and under 69,000 volts. TrizecHahn Br. at 22-23, BOMA Br. at 16-17. The evidence does not support this contention. ComEd's computation of the credit provided in Alongi-Kelly Sur., ComEd Ex. 50.0 CR, Att. B, appropriately uses maximum demands to compute, through the use of integral calculus, the difference in the total \$/kW marginal distribution investment costs to provide standard service to load served at or above 69,000 volts versus load served at lower voltages. Alongi-Kelly Tr. 1299:16-1302:17; Alongi-Kelly Sur., ComEd Ex. 50.0 CR, Att. B. IIEC, which previously

questioned the accuracy of ComEd's calculation of the marginal cost credit, (Chalfant Dir., IIEC Ex. 2.0 CR, p. 19:1-11), no longer does so, although it suggests an alternative average replacement cost approach. IIEC Br. at 24. DOE verifies the accuracy of ComEd's calculation, stating that it "is certain that the credit has been calculated correctly...." DOE Br. at 15.

TrizecHahn's contention that the calculation is somehow incorrect because "there are many customers served at or above 69 kV who actually have a higher cost of service than those served below 69 kV" is simply incorrect. TrizecHahn Br. at 21. There are not "many" customers in this situation. The evidence indicates that there are only eight. Alongi-Kelly Sur., ComEd Ex. 50.0 CR, Att. B, p. 2. Moreover, in any group of customers, there will always be some who cost more and some who cost less to serve than the weighted average cost of the group. Alongi-Kelly, Tr. 1259:12-1260:4. For example high rise customers in the City of Chicago cost substantially more to serve than other customers in their class. *Id.* This basic fact has nothing to do with the correctness of ComEd's HVDS credit calculation.

TrizecHahn's additional complaint that there is no "discernible pattern to the scatter diagram showing marginal distribution investment for below 69 kV customers....," (TrizecHahn Br. at 21), does not support modification of the calculation of the credit either. ComEd considered the absence of such a pattern and addressed it by using a weighted average cost (\$409.58/kW) for those customers. Alongi-Kelly Sur., ComEd Ex. 50.0 CR, Att. B, p. 2.

TrizecHahn's further contention that ComEd's unwillingness to accept an embedded cost-based credit supports rejection of ComEd's marginal cost-based credit, TrizecHahn's Br. at 14, is completely illogical. ComEd has correctly calculated and supported its proposed HVDS credit, and its disagreement with an embedded-cost approach, which Staff now advocates, Staff

Br. at 101, has nothing to do with the propriety of the marginal cost-based credit ComEd proposes.

c. Allocation of Costs to Other Customers

The ARES Coalition, TrizecHahn, and BOMA contend that Rider HVDS will result in “rate shock for non-qualifying customers.” ARES Coalition Br. at 94-95; TrizecHahn Br. at 23; BOMA Br. at 16. In an effort to support this contention, BOMA provides a table ostensibly demonstrating that customers in the over 10MW class who are ineligible for the credit will experience a 68.98% rate increase. BOMA Br. at 15, Table 1. The information in BOMA’s table is simply inaccurate. It is based on the outdated \$2.65/kW HVDS credit, rather than the actual \$1.69/kW credit proposed by ComEd. It also uses a Distribution Facilities Charge of \$3.05/kW rather than the actual \$2.58/kW proposed charge. Although BOMA acknowledges the correct credit and charge amounts proposed by ComEd, (BOMA Br. at 14), it nonetheless persists in presenting comparisons based on inaccurate information. Further, ComEd provided a specific customer calculation in its surrebuttal testimony whereby it confirmed that the non-HDVS customer did not experience rate shock because of the CTC offset and actually paid less. Juracek Reb., ComEd Ex. 41.0, pp. 15:374-16:393.

It is no surprise that customers who have benefited from subsidies will experience higher rates when those subsidies are reduced or eliminated. That is no reason to continue the subsidies. As the DOE correctly observes, the allocation of the cost of Rider HVDS to other customers merely means that “they are now paying the full cost of providing them with service” (DOE Br. at 17) which is exactly what they should be paying. Deferring the date on which customers pay these costs by two years, as IIEC proposes (IIEC Br. at 25), is inappropriate. As DOE aptly observes “this simply amounts to a requirement that high voltage customers be required to continue to subsidize lower voltage customers for another two years.” DOE Br. at 16.

d. Exemption From Rate RCDS Facility Charges

DOE requests that the sole 345 kV load customer on ComEd's system be afforded rate treatment like that proposed for IPPs. DOE Br. at 15-20. Because of the unique characteristics of this customer, severed at this specific voltage, ComEd does not object. Clair-Crumrine, Tr. 1057:20-1058:21.

e. Adoption Prior to Bundled Rate Tariff Change

BOMA and the ARES Coalition argue that the cross subsidies that Rider HVDS eliminates should be allowed to continue until 2005 when comparable rate design changes can be made to bundled rates. BOMA Br. at 17-18; ARES Br. at 96. As ComEd explained in its initial brief, there are and will be differences between bundled rate design and delivery services rate design, but that is no reason to ignore unfair cross subsidies in delivery services rates. ComEd Br. at 33-34. Those subsidies can be addressed now. Similar problems in bundled rates cannot.

3. Rider ISS

a. Pricing

Certain parties disagree with ComEd's proposed PPO pricing, objecting to ComEd's 10% additional charge, or to its use of PPO rates as a base and propose alternative pricing methods, all of which should be rejected. The ten percent additional charge provides an incentive to residential customers to seek out new suppliers and prevents gaming. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 8:177-9:195. In their initial briefs, the IIEC asserts that Rider ISS should be based upon hourly energy prices, while the Staff asserts that Rider ISS should be based upon bundled rates, plus 10%. Use of HEP would subject residential customers to volatile market shifts, and would be costly and difficult to implement from a billing perspective. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 6:120-7:162. Use of bundled rates results in

unnecessary differences between residential and nonresidential customers, and was recently rejected by the Commission. *Central Illinois Public Service Co., et al.*, Docket No. 00-0802, (December 11, 2001) pp. 50-51. ComEd demonstrated that its pricing of Rider ISS on PPO rates, with a 10% additional charge, is the proper pricing methodology. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, pp. 25:584-26:604. Staff agreed that, if the Commission rejected its proposal, ComEd's proposed pricing methodology is an appropriate alternative. Harden, Tr. 2169:17-21.

b. Commission Authority to Alter ComEd's Proposal

The IIEC and ARES assert that the Commission may modify any tariff proposed by ComEd. Though that principle is generally true, Rider ISS is not a delivery services tariff and is not required by the Act. Therefore, ComEd cannot be ordered to provide this service at all. 220 ILCS 5/16-103(e). Nonetheless, ComEd agreed voluntarily to provide this service, but only on terms that ComEd proposed, which ensure it fair cost recovery. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, pp. 24:547-64, 25:570-77; Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 10:223-26. Though the IIEC claims that ComEd may not withdraw a tariff without Commission approval, the IIEC does not dispute that ComEd may decline to extend this voluntary service offering to residential customers, or on different terms than those to which ComEd agreed.

4. Other Customer Class Definition Issues

Although Staff witness Michael Luth previously advocated establishment of a new high voltage rate class, Staff's brief now supports ComEd's approach of eliminating cross subsidization through an HVDS credit. Staff's Br. at 101. The ARES Coalition continues to argue for "a full set of rates based upon voltage levels" (ARES Br. at 91-92), and their argument should be rejected for the reasons discussed in ComEd's Initial Brief. ComEd's Br. at 123.

6. SBO Credit

ComEd's proposed Single Bill Option ("SBO") credit is appropriately calculated based on net costs that ComEd will avoid when RESs elect the SBO, not on embedded costs. ComEd Br. at 124-27. The ARES Coalition, NEMA, and Staff all note that the proposed SBO credit is \$0.03, which is 52 cents less than the existing SBO credit. ARES Br. at 102; NEMA Br. at 9; Staff Br. at 105. The ARES Coalition calls this as a reduction of 94.5%, mathematically observing that the current credit is 1,833% of the proposed credit. ARES Br. at 102. These percentages say nothing improper about the calculation or propriety of the proposed credit. Nor does anything in the record. Rather, the record shows that under an avoided cost approach, a small credit is to be expected (Gordon Dir., ComEd Ex. 2.0, pp. 21:577-23:609), and in this case, the proposed credit is actually generous, ComEd Br. at 105-07. Indeed, the Act never refers to any credit; whatever it is, positive, negative, or zero, simply flows from the actual costs. The record also shows that any excess above the credit produced under an avoided cost approach is simply a subsidy. Gordon Dir., ComEd Ex. 2.0, pp. 20:501-13, 24: 615-19; Makholm Dir., ComEd Ex. 15.0, p. 8:234-41; Gordon Sur., ComEd Ex. 44.0, p. 6:149-60.

Staff also claims that ComEd's proposed SBO credit favors the utility, arguing that alternative suppliers must compete on the basis of their full costs, while utilities will compete on a "more relaxed" standard of avoided costs. Staff Br. at 105-06. This claim is misguided. Under the proposed SBO credit, both ComEd and alternative suppliers will compete on the basis of their marginal costs – that is, the identical standard. Makholm Reb., ComEd Ex. 34.0, p. 9:209-18. Indeed, contrary to Staff's suggestion, it is an SBO credit based on embedded costs that causes favoritism – namely, a significant subsidy to alternative suppliers. Gordon Dir., ComEd Ex. 2.0, pp. 20:501-13, 24:615-19; Makholm Dir., ComEd Ex. 15.0, p. 8:234-41; Gordon

Sur., ComEd Ex. 44.0, p. 6:149-60. All the while, ComEd will keep paying costs it cannot recover.

Staff and the ARES Coalition both suggest that adopting the proposed credit will harm competition. Staff Br. at 106-07; ARES Br. at 102. But the record is clear that using an avoided cost approach will promote efficient competition and economic efficiency. Gordon Reb., ComEd Ex. 21.0, pp. 7:165-8:181; Gordon Dir., ComEd Ex. 2.0, p. 3:74-80; Makholm Dir., ComEd Ex. 15.0, p. 2:53-72. The record is equally clear that using an embedded cost approach will damage competition, permitting inefficient competitors to enter and remain in the market, which ultimately will harm society and customers through market distortions and higher prices. Gordon Reb., ComEd Ex. 21.0, pp. 7:157-8:181; Gordon Sur., ComEd Ex. 44.0, p. 5:112-14; Makholm Dir., ComEd Ex. 15.0, pp. 3:73-81, 9:272-83; Gordon Dir., ComEd Ex. 2.0, pp. 4:94-100, 18:474-89, 23:612-32. Thus, ComEd's proposal will not "gut" the market for unbundled billing; rather, it will provide all competing firms the appropriate opportunity to compete on a level playing field. Gordon Reb., ComEd Ex. 21.0, p. 8:188-90.[†]

The ARES Coalition not surprisingly wants to maintain the subsidy provided by the current embedded cost based SBO credit (ARES Br. at 103) – they receive the subsidy. They may be "pro-competitor," but they are not "pro-consumer" or "pro-competition." Gordon Dir., ComEd Ex. 2.0, p. 24:656-60. Competition cannot be tilted – by subsidies or other means – to protect inefficient firms. Gordon Reb., ComEd Ex. 21.0, pp. 2:32-3:66. Consumers ultimately pay for the inefficiencies wrought by subsidization. Gordon Dir., ComEd Ex. 2.0, p. 24:649-60.

[†] Staff's concern about Dr. Makholm's testimony concerning natural monopolies (Staff Br. at 105-07) is unfounded. The point of competition is promote social welfare through efficiency. Although there is no evidence to suggest that a natural monopoly for an unbundled service exists here, natural monopolies can occur where it is most efficient for one entity to provide that service. In such instances, society still benefits. Makholm Dir., ComEd Ex. 15.0, p. 9:266-71.

In essence, the ARES Coalition is making a classic “protect an infant industry” argument – a theory that has fundamental difficulties and about which economists have long been skeptical. Gordon Dir., ComEd Ex. 2.0, p. 25:661-76; Gordon Reb., ComEd Ex. 21.0, p. 8:182-88 & n.6.

Staff also disputes the fact that a utility is more efficient than a competitor where the utility’s avoided cost for a service is less than the competitor’s cost for providing that service. Staff Br. at 106. Staff’s contentions here are confused. The proper analysis for efficient use of resources is a marginal cost analysis: if the utility’s avoided cost from not providing the service is less than the competitor’s incremental cost of providing that service, then the utility is more efficient and should provide the service. Gordon Dir., ComEd Ex. 2.0, p. 19:514-23. The utility’s embedded costs are separate; while the utility has a legal right to recover those costs as part of its delivery rates, 220 ILCS 5/16-108, they are not relevant to the above marginal analysis. Gordon Dir., ComEd Ex. 2.0, p. 12:320-33; Gordon Reb., ComEd Ex. 21.0, p. 6:144-51; Makholm Sur., ComEd Ex. 55.0 CR, p. 7:162-77.[†]

NEMA and Staff claim that ComEd’s SBO credit proposal also conflicts with Commission precedent. NEMA Br. at 9-10; Staff Br. at 107. As explained above, the Commission must decide this case on the law and the record developed in this proceeding. The record in this proceeding shows, beyond dispute, that ComEd’s avoided costs are less than the average embedded costs and, therefore, that if an avoided cost credit is not approved, ComEd will not and cannot recover its delivery services costs. Clair-Crumrine Dir., ComEd Ex. 12.0 CR, p. 41:929-42; Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 2:29-3:53; Alongi-Kelly Dir., ComEd Ex. 13.0 CR, p. 38:827; Makholm Reb., ComEd Ex. 34.0, p. 6:145-47. This is plainly illegal. Past Commission orders approving embedded costs have been affirmed on appeal

[†] For similar reasons, GC’s observation that ComEd’s avoided costs and the delivery rates for billing are not the same, GC Br. at 83, is of no consequence. There is no reason why they should be.

because the Appellate Court found that this fact had not been proven. *Commonwealth Edison Co. v. Illinois Commerce Comm’n*, 322 Ill. App. 3d 846, 854, 751 N.E.2d 196, 203 (Ill. App. 2001); ComEd Br. at 126-27. It is proven here.[†]

The ARES Coalition claims that the Commission should not allow ComEd to be paid for a function it no longer performs. ARES Br. at 103. They err. An avoided cost approach does just this. Other than to the extent that a customer’s taking unbundled billing from an alternative supplier reduces ComEd’s total billing costs (for which ComEd properly proposes to provide a credit equal to that reduction), ComEd proposes to recover exactly its costs – not a penny more. Moreover, ComEd continues to be the provider of last resort. ComEd Br. at 124-27. It continues to provide the service of standing by to bill all customers, and incurs real costs to provide that service which it is entitled to recover.

As a result, the ARES Coalition’s suggestion that unbundled customers should not be “penalized” for switching to alternative suppliers (ARES Br. at 103) is wrong. ComEd’s proposed SBO credit does not penalize such customers. Of course, at the same time, it does not provide them with a windfall subsidy. Rather, it creates a level playing field, which will promote competition and benefit society and customers. Makhholm Sur., ComEd Ex. 55.0, p. 14:330-38.

Finally, ComEd notes that its embedded cost study – which ComEd does not propose as the basis for its delivery rates – has been updated for use of a Value Added Network. Alongi-Kelly Reb., ComEd Ex. 32.0, Att. F, p. 3. Because ComEd must be able to transmit information

[†] NEMA’s advocacy of embedded costs as a way to build “shopping credits” (NEMA Br. at 10) should be rejected, as there is no authority for it under the Act, it is not at issue in this proceeding, and the Commission already has addressed various unbundled services in a separate proceeding, Docket No. 99-0013. Juracek Reb., ComEd Ex. 20.0, p. 31:741-46; Clair-Crumrine Reb., ComEd Ex. 31.0, pp. 36:829-37:846.

to and from potential RESs, through their information systems, a credit for Internet exchange is inappropriate.

7. Metering Service Charge (Credit)

As ComEd explained in its Initial Brief at 127-29, the metering service charge (credit) should be calculated on the net costs that ComEd will avoid when customers elect unbundled meter service, not on embedded costs. Many of the arguments raised against ComEd's proposal – that it is significantly lower than the current one (ARES Br. at 104; NEMA Br. at 9 & n.8; Staff. Br. at 111); that it favors the utility with a “more relaxed” standard (Staff Br. at 112); that it will harm competition (Staff Br. at 112-13; ARES Br. at 104-07) that it is contrary to Commission precedent, (NEMA Br. at 9-10; Staff Br. at 113) and that ComEd should not get paid for a function it no longer performs (ARES Br. at 106) – are the same arguments raised against ComEd's SBO credit proposal, and are meritless the same reasons (*see* Section II.G.6).

Other arguments against the proposed metering service charge (credit) fare no better. The ARES Coalition claims that ComEd's proposal amounts to a “bait and switch,” and even goes as far as to say that the proposal would have a “devastating anti-competitive impact upon the development of competition in metering services.” ARES Br. at 103. Contrary to this hyperbolic rhetoric, ComEd's proposal in no way constitutes a “bait and switch.” A “bait and switch” is luring in a target with something appealing, and then once the target has been lured, switching to something less appealing for the target but more rewarding for the baiter and switcher. But ComEd has done no baiting here; it filed metering tariffs to comply with the Commission's Final Order in Docket No. 99-0013, which was entered in October 2000. Nothing in that Order or any other authority prohibits ComEd from exercising its legal right to petition for the rates for which it seeks approval in this proceeding. Further, there is no evidence in the record suggesting that any current or alternative meter service provider has relied on the size of

the current charges (credits). In any event, if an alternative provider is efficient, then it should have no problem competing using ComEd's proposed avoided cost based metering service charges (credits).

In addition, as a practical matter, with only one alternative MSP having been certified (ARES Br. at 105), and with no customers taking unbundled metering service (ComEd Br. at 129), the suggestion that ComEd's proposal will have a "devastating anti-competitive impact" borders on ridiculous. More generally, as the above discussion of the proposed SBO credit makes clear, using avoided costs will promote efficient competition in metering services.

Staff's criticism of Dr. Makholm's consideration of the impact of an embedded cost approach as "narrow" and indicative of a lack of sympathy for consumers (Staff Br. at 114) is off the mark and actually exactly backwards. As ComEd explained in its Initial Brief at 127-28 and Staff recognizes with surprising nonchalance, the embedded cost approach will deny ComEd cost recovery and will require cross subsidies from customers who do not elect unbundled metering service – both plainly illegal results. Moreover, as the record overwhelmingly shows, using embedded costs leads to inefficiency, which ultimately harms society and consumers. Gordon Dir., ComEd Ex. 2.0, p. 19:506-13. There are multiple "[l]osers" from the inefficiency of excessive credits – including customers and the process, as well as the utility. Makholm Dir., ComEd Ex. 15.0, p. 9:272-83. As a result, the embedded cost approach, while perhaps benefitting the relative few who receive subsidies, harms the many. It is thus the embedded cost approach – not the avoided cost one – that focuses on narrow interests and lacks sympathy for consumers overall.

The ARES Coalition also claims that the proposed charge (credit) will not permit RESs like AES New Energy to use an MSP to obtain certain "value-added services." ARES Br. at 105.

Though ARES do not define “value added services,” all services other than metering service, as defined by the Commission, are unregulated, competitive services that can be obtained from any entity providing such services. More fundamentally, this argument ignores the fact that the MSP credit has nothing to do with the price or attractiveness of a competitive, value-added service. If an ARES is willing to pay a competitive price, a supplier will respond.

The ARES Coalition also claims that ComEd has not shown how it arrived at the proposed credit of \$0.98 per month, and how it accounted for various savings that purportedly would arise from the departure of a customer onto unbundled metering. ARES Br. at 105-06. But, the record is clear how ComEd calculated this credit. Alongi-Kelly Dir., ComEd Ex.13.0 CR, pp. 31:688-32:702 & Att. P; Alongi-Kelly Reb., ComEd Ex. 32.0, 22:463-23:469. And the record is equally clear that this calculation was proper and correct, appropriately accounting for avoided costs. Alongi-Kelly Reb., ComEd Ex. 32.0, pp. 22:463-24:497; Alongi-Kelly Sur., ComEd Ex. 50.0 CR, pp. 1:19-2:30, 10:194-11:213.

The ARES Coalition finally claims that ComEd’s proposed use of a single metering service charge (credit) for all customer classes is unjustified because the cost of meters and services charges can vary. ARES Br. at 106. This claim is unfounded, however: the standard metering service charges vary by customer class depending upon the type of standard meter applicable to the class. Alongi-Kelly Reb., ComEd Ex. 32.0, p. 23:470-84.

8. Rider TS – Transmission Service

ComEd’s Rider TS performs three independent functions. With the exception of a single rate design issue raised by IIEC, no party takes issue with the: (1) pass-through to Rider PPO and Rider ISS customers of the transmission services and ancillary transmission services charges incurred by ComEd on their behalf; or (2) credit to delivery services customers’ CTCs of those

transmission services and transmission ancillary services charges of an RTO corresponding to the transmission charges currently credited by ComEd. *See* ComEd Br. at 129-35.[†]

IIEC argues that ComEd should pass through transmission costs at different rates for customers in different RCDS classes. IIEC Br. at 38-40. ComEd's initial brief explains why this would be inappropriate: the OATT lacks such customers classes. Rates under the OATT and, thus, ComEd's costs, will not vary depending upon a customer's Rate RCDS customer class. ComEd Br. at 132. Favoring large customers' classes under Riders ISS and PPO, while their actual unit transmission cost is identical to other customers, is a naked and unjustified request for a subsidy. ComEd Br. at 131-32. Moreover, the evidence does not show that ComEd's proposal will increase transmission charges to larger customers. *Id.* Finally, IIEC's observation that the CTC credit for transmission differentiates between customer classes misses the point. The CTC has differing impact across classes; unlike simply passing-through equal charges to PPO and ISS customers, it is appropriate mathematically to take these differences into account.

The remaining arguments regarding Rider TS focus on the third function of the Rider: to allow ComEd to bill end users for their use of transmission service provided by an RTO if their RES fails to pay for these services on their behalf. The end user is liable because it is an OATT customer; ComEd's proposed tariff simply allows it to bill for the OATT services, on behalf of the RTO transmission provider. Sterling Sur., ComEd Ex. 56.0, p. 2:29-33. ComEd's proposal is widely misunderstood and mischaracterized. In particular:

- Rider TS does not change the retail customer's ultimate responsibility for transmission charges. Retail customers are the Eligible Customers and the users of transmission services under the OATT, are fully liable for their cost under federal law and the OATT, regardless of whether the relevant section of ComEd's proposed Rider TS is accepted. Sterling Sur., ComEd Ex. 56.0, pp. 4:76-79, 6:126-29. No provision, or revision, of ComEd's Illinois rates

[†] Rider TS is "RTO neutral" and will function with any RTO proposed for the midwest.

can “force the transmission provider to forfeit the right to look for payment to the Eligible Customer.” Sterling Sur., ComEd Ex. 56.0, p. 4:78-79. [†]

- Rider TS does not affect ComEd’s rights while ComEd remains the transmission provider. ComEd accepted Staff’s suggestion that Rider TS be clarified to state that it will only become effective when an RTO is operational. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 32:718-25. ComEd’s proposal also does not create or alter the right of an RTO transmission provider to look to retail customers for transmission services and ancillary transmission services charges. That right exists in the RTO OATT. ComEd Br. at 129-30.
- What Rider TS does is allow ComEd to bill for transmission services, on behalf of the RTO, after the RTO becomes the transmission provider. Sterling Sur., ComEd Ex. 56.0, p. 2:31-33. “All ComEd’s proposal does is allow [an RTO] to use ComEd’s retail billing system to do so in a practical, lower cost manner.” Sterling Sur., ComEd Ex. 56.0, p. 6:128-29.
- ComEd’s proposal does not financially benefit ComEd, but is a pro-competitive means of reducing collection costs and easing an unnecessary credit burden on RESs. *See* ComEd Br. at 133.

ComEd also proved that this portion of Rider TS is desirable. *See* ComEd Br. at 133-35.

Staff’s brief claims that the benefit to the market is “irrelevant” and can be achieved in other ways is without support in the record. The evidence shows that ComEd’s proposal offers an opportunity to reduce needless RES credit costs. *Id.*

In response, IIEC, GC, and Staff argue at length that this portion of Rider TS is an attempt to “maintain the requirement in its delivery services tariffs (DSTs) that holds retail customers financially responsible for the unpaid portion of their RES’ (or other entity’s) transmission bill” (Staff Br. at 125; *see* GC Br. at 97-100), or to prohibit a RES from negotiating liability for transmission with their customers. IIEC Br. at 36-38. These arguments mischaracterize Rider TS and ignore controlling provisions of the OATT. As noted above, end users are liable for transmission charges under the OATT. That liability is not created by state tariff. The record shows:

[†] Although GC is one of the parties that contests what it characterizes is ComEd’s proposal to “make RCDS customers liable for FERC transmission charges incurred by the retail customers RES” [sic] (GC Br. at 98), it also admits that, in fact, under the OATT, the transmission provider can proceed against the “transmission customer and against the retail customer -- independently of Edison’s DST.” *Id.* at 99.

- RESs are not Eligible Customers for retail transactions regardless of what the RES and the customer agree. Sterling Sur., ComEd Ex. 56.0, pp. 2:34-3:56, 4:72-75; Sterling Reb., ComEd Ex. 36.0, p. 3:72-74; Sterling, Tr. 2355:11-18.[†] RESs can and do act as a Transmission Customer on the eligible retail customer's behalf. The OATT is clear on this. Sterling Sur., ComEd Ex. 56.0, p. 4:72-75. Indeed, the "retail service" proviso in the eligibility section of the OATT emphasizes that transmission service need not be offered to entities, like RESs, who are not required by state law to be offered unbundled retail service. Sterling Sur., ComEd Ex. 56.0, p. 3:57-68; OATT, Original Sheet Nos. 13-14 §1.11(i). Indeed, were it otherwise, a RES could obtain unbundled retail transmission service regardless of state decisions on open access. The RES would merely assert it was itself eligible under the federal tariff. *See, e.g.*, OATT, Original Sheet Nos. 107-111 §§22.1, 22.2, 23.1.
- The inability of a RES to be an Eligible Customer is not open for debate. The OATT is a FERC tariff and FERC has confirmed this fact. Order No. 888-A, 78 FERC ¶ 61,220, Slip Op. at 111-12 (Mar. 4, 1997) (*quoted in* Sterling Sur., ComEd Ex. 56.0, p. 3:60-68).
- To the extent that eligibility to take transmission service is at all a function of state law, it is clear that transmission services and transmission ancillary services provided by a utility are delivery services. Sterling, Tr. 2397:8-12; *Commonwealth Edison Co.*, Docket 99-0117 (August 26, 1999), p. 55. The Act is equally clear that delivery services are to be offered directly to retail customers and not to RES, with a very few specific exceptions not relevant here (*e.g.*, standard billing under SBO). 220 ILCS 15/16-104(a). No provision of the Act authorizes the Commission to order ComEd to offer retail delivery services to RESs. The Commission is expressly prohibited from ordering utilities to offer services beyond those previously offered or called for by the Act. 220 ILCS 5/16-103(e).
- Illinois policy is to offer delivery services directly to end users, not middlemen. Indeed, the provision of delivery services directly to retail customers, and not to re-sellers, is a key feature of the Act. *E.g.*, 220 ILCS 5/16-104.
- Given that transmission services provided by a utility are delivery services, there is nothing unfair or inequitable about using delivery services billing and collection systems, and remedies including disconnection, to secure payment for transmission services that have been provided and used by customers at the least cost. That is a benefit for the market and for consumers generally. Sterling Reb., ComEd Ex. 36.0, p. 4:75-96.
- To allow the RES and the customer to decide among themselves who will be liable for tariffed transmission charges on a case by case basis is patently unfair. Sterling Sur., ComEd Ex. 56.0, pp. 4:80-5:101. This notion:

is problematic for the same reason that any two debtors are not allowed to negotiate their liability to an absent creditor among themselves. Liability for charges is not their right to negotiate away. ... [C]ustomers and their RESs are free to negotiate *as among themselves* mutually agreeable terms and conditions for payment of

[†] "Eligible Customer" and "Transmission Customer" are specific, technical terms under the OATT. OATT, OATT, Original Sheet Nos. 13-14 § 1.11 and Original Sheet Nos. 24-25 § 1.45. Every transmission transaction requires an Eligible Customer.

transmission services used by the end-use customer. However, the existence of such terms and conditions in a contract between a RES and an end-use customer does nothing to alter or supercede the terms and conditions contained in the OATT which is an agreement between the Transmission Provider and the Eligible Customer. Sterling Sur., ComEd Ex. 56.0, p. 4:84-92.

- End user liability is not simply back-up security for RESs who may not be credit-worthy, and that therefore can or should be jettisoned if a RES is sound or posts other security. Indeed, this notion turns the OATT on its head. Credit security is the back-up, to be used when the liable parties -- the Eligible Customer and the Transmission Customer (often the same entity) -- do not pay. What Rider TS does is allow the RTO an inexpensive and cost-effective means of collecting transmission charges without requiring needlessly great credit security.

Several parties also argue that retail customers should not be liable for transmission charges because they may not understand or be able to control the details of transmission operations. IIEC Br. at 38; Staff Br. at 126-27; GC Br. at 98-99. These arguments are no reason to reject any portion of Rider TS. Retail customers are liable under the OATT. Rider TS does not change that; Rider TS is a billing and collection tool only. Moreover:

- Consumer education arguments actually support Rider TS. Under current law, the rule is simple: a retail customer is liable for the transmission services it uses regardless of its choice of a RES. It is less likely that customers will understand a host of different rules contained in complex, unregulated RES contracts, that differ for each RES and, potentially, for each customer, and which will be subject to interpretation by the transmission provider, FERC, and/or a court. Moreover, nothing in ComEd's proposal (or the OATT) prevents a retail customer from negotiating special credit security provisions with its RES. For example, in Staff's "hypothetical" about the failure of "End-Run" (Staff Br. at 128-29), the customer remains free to ask the RES to post a bond or other security, or to seek other terms that protect it against End-Run taking its money without paying the transmission bill. Realistically, these types of negotiations will not happen often, but Rider TS does nothing to inhibit them.
- Consumers need not understand details of transmission operations such as load forecasting, scheduling, and the use of ancillary services (the examples cited by Staff) to be fairly liable for transmission costs. Consumers have been liable for transmission costs as part of bundled rates for decades. Rider PPO and ISS customers are charged for transmission arranged by ComEd, regardless of whether they understand how ComEd manages transmission procurement. There is nothing unfair in the fact that other unbundled customers are likewise liable for transmission charges. Indeed, these customers actually are the best off: they have chosen their own RES and, presumably, considered its financial strength.

Finally, Staff alone also appears to make a third argument relating to end user liability for transmission charges, claiming that retail customers are liable for transmission charges because ComEd's Illinois tariffs provide that RES acts as their agent. Staff Br. at 127-28. Staff errs. No agency relationship is required for a retail customer to be liable for transmission charges. As noted above, a retail customer is liable for transmission charges because it is the Eligible Customer under the OATT, and because it is the actual user of the transmission services. The agency relationship established under Rates RCDS and RESS simply allows the RES to automatically act as an agent for all of the retail customers it supplies with power and energy. *See* Rate RESS, Ill. C.C. No. 4, Sheet No. 172. This is a pro-competitive tariff provision. ComEd has not sought to change it in any way in this Docket, and it would be extremely disruptive to the market to do so, especially given that it has nothing to do with Staff's concern.

**9. 24-Month Return to
 Bundled Service Requirements**

ComEd's rates and Plan provide that a residential customer that returns to bundled service be prohibited from returning to delivery services for a period of twenty-four months. Alongi-Kelly Dir., ComEd Ex. 13.0 CR, pp. 4:85-5:88 & Att. C at 2nd Revised Sheet No. 109, Original Sheet No. 133.2, 2nd Revised Sheet No. 159. Nicor argues that this period be limited to 12 months. Nicor Br. at 3. Nicor's suggestion is plainly contrary to the Act, and must be rejected. As noted in ComEd's initial brief, Section 16-103(d) of the Act (220 ILCS 5/16-103(d)) specifically provides that, for residential and small commercial customers, ComEd "shall be entitled to impose the condition that such customer may not elect delivery services for up to 24 months thereafter." *Accord* Juracek Reb., ComEd Ex. 20.0, p. 32:766-70.

Staff acknowledges ComEd's right, under the Act, to establish a 24-month period. Staff Br. at 115. However, Staff states that in its view this is a "harsh penalty." *Id.* The evidence

shows that the 24-month period is not a penalty, but a legitimate means or helping to mitigate (albeit, incompletely) uncompensated supply risk. Juracek Reb., ComEd Ex. 20.0, p. 41:969-42:979. Indeed, the Act, in specifically authorizing a 24-month period, implicitly determined that this was the period that properly balanced the need to protect utilities with the desire to allow efficient movement to competitive providers. Staff also asks the Commission to alter cosmetically ComEd's tariff to state that the 24-month period is "permitted by" the Act rather than "in accordance with the Act." Staff Br. at 116. This revision is unnecessary. The 24-month period plainly is in accordance with the Act.

10. Rider 25

The arguments of the ARES Coalition and BOMA about the effect of ComEd's proposals on Rider 25 customers were already answered by ComEd. BOMA Br. at 18-20; ARES Br. at 107-08. ComEd demonstrated that Rider 25 customers are participating in the open access system, that the opportunity for savings will not be eliminated by ComEd's proposals in this case, and that the possibility that some Rider 25 customers may choose the favorable bundled service rates available to them rather than electing to take delivery services is not an indication that adverse customer impacts have resulted. ComEd's Br. at 136-38. Their contention that ComEd's delivery services rate design must "mirror the rate design under the bundled rate" (BOMA Br. at 19-20) is simply wrong as a matter of law. Bundled rates and rate design are frozen and cannot be changed. 220 ILCS 16-111(a). Delivery services rates are not frozen and should be designed to fully recover costs and reduce cross subsidies of the type that ComEd has addressed in this case. And, as with customers in other delivery services rate classes, positive CTCs will be available to Rider 25 customers to offset increases in the cost of providing delivery services. *See* Section II.G.1.c.

11. Other Topics

IIEC acknowledges that its concerns regarding the continued availability of ComEd's pro-competitive retail energy imbalance service were addressed in Ms. Sterling's testimony. IIEC Br. at 39-40; *see* Sterling Sur., ComEd Ex. 56.0, pp. 6:130-7:151. IIEC's final request, that the Commission continue to remain actively involved in the RTO energy imbalance debate, is simply not germane to this Docket or to any tariff under review.

III. Terms and Conditions Issues

A. SBO Credit Eligibility (Customers With Past Due Bundled Service Balances)

The ARES and GC erroneously claim that ComEd's proposal to prevent (residential and nonresidential) customers with past due bundled balances owed to the utility from taking service under ComEd's Rider SBO lacks support in the record and is anti-competitive. ARES Br. at 109-10; GC Br. at 88-89. To the contrary, ComEd explained at some length the reasons for limiting SBO eligibility and the significant costs imposed by dual billing (approximately \$225.00 per account). Clair-Crumrine Dir., ComEd Ex. 12.0 CR, pp. 34:779-37:862; Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 41:941-42:957; Alongi-Kelly Reb., ComEd Ex. 32.0, Att. F, n.3. Similarly, the "anti-competitive" refrain is misplaced. Customers are eligible for the SBO as soon as the past due bundled services balance is paid in full, and customers may take delivery services from a RES even while a bundled services balance is owed to ComEd. In addition, customers with legitimate billing disputes remain eligible for the SBO, and the SBO credit. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 40:911-41:928.

Staff has no objection to ComEd's proposal, but requests that ComEd maintain records of the number of customers who attempt to switch to SBO while owing a bundled balance, and the reason for the balance. ComEd has no objection to Staff's request at this time.

B. Enrollment Issues

A number of intervenors have proposed that the Commission permit customers to enroll with RESs electronically, and NEMA alone proposes that customers also be permitted to enroll telephonically. Telephonic enrollments are clearly inconsistent with the requirements found in the Illinois Consumer Fraud and Deceptive Business Practices Act, 815 ILCS 505/2EE ("Section 2EE"), which requires written authorization to effect a change of electric service provider, and should be rejected. Though other parties are quick to assert that recent Illinois and federal legislation pertaining to electronic signatures pre-empts Section 2EE, reconciling the new legislation with the specific disclosure requirements of Section 2EE may prove to be more difficult than the intervenors realize or are willing to admit. *Clair-Crumrine Reb.*, ComEd Ex. 31.0 CR, pp. 51:1160-52:1194.

Intervenors note that a prior Commission order permitted internet enrollment with a gas company. However, it is not clear whether there was any analysis of the particular requirements of Section 2EE as it relates to electronic signatures. ComEd is particularly concerned with this issue in that, if any problems surface as a result of electronic signatures, it will be ComEd that state and federal officials turn to and scrutinize for possible violations of Section 2EE.

D. Off-Cycle or Non-Standard Switching for Residential Customers

The GC contends that the Commission should require ComEd to perform off-cycle switches on a "best efforts" basis, and requests that a clear interpretation of applicable performance criteria be established. GC Br. at 90. ComEd is willing accommodate off-cycle

switching by residential customers on ISS, except in situations in which a RES attempts to remove a large number of customers from Rider ISS at one time. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, p. 46:1040-47. No party disputes that unscheduled meter readings to accommodate off-cycle changes in supplier would result in increased meter reading costs for ComEd, and no party offered any alternative performance criteria. ComEd's proposal is reasonable and appropriate at this time, and should be approved. Staff agrees. Staff Br. at 123.

E. General Account Agency Issues

The ARES object to the use of a standard agency form for agents in ComEd's service territory, contending that it is an unnecessary level of bureaucracy. ARES Br. at 110-12. With the number of agents in ComEd's territory at 16 and rising, as recognized by Staff, "it is reasonable for utilities to be able to show that they have informed customers of the risks inherent in using account agents." Staff Br. at 124. In fact, "Staff would prefer that each utility adopt ComEd's general approach." Schlaf Dir., Staff Ex. 10.0, p. 9:231.

Staff prefers that customers receive duplicate disconnection notices and that duplicate notice fees be included in the revenue requirement, rather than charged the customer requesting the duplicate notice. Staff Br. at 124-25. A signed agency form signifies the customer's desire that the agent act on behalf of the customer in all dealings with ComEd. Staff's proposal unnecessarily interferes in the customer-agent relationship, and shifts costs away from the cost-causers, in violation of basic ratemaking principles. Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 49:1124-50:1145.

F. Value-Added Aggregation Services

Staff recommends that certain contracts for Customer Aggregation and Targeted Consulting Services between ComEd and other entities be filed with the Commission within 30 days of the contract date. Staff Br. at. 132-33. Under Staff's proposal, ComEd would be

required to file all contracts ComEd enters into with any of its affiliates, as well as filing the three largest dollar value contracts entered into between ComEd and any non-affiliated entity.

There is no basis under the Act that requires ComEd to file such contracts for competitive services. ComEd mentioned possible service offerings designed to facilitate customer aggregation, in the hopes of obtaining feedback as to whether such services would be helpful to market participants. Consequently, there are no contracts available for review. If, ultimately, ComEd does provide customer aggregation and targeted consulting services, it will do so as a voluntary service offering that is not required or performed under any tariff offering. In addition, requiring ComEd to file such contracts, while competing providers of similar services are not subject to such regulatory scrutiny, is inconsistent with the Act's provisions. 220 ILCS 5/16-116(b); *see* Clair-Crumrine Reb., ComEd Ex. 31.0 CR, pp. 37:848-40:909.

G. Collection of FERC Charges Under DSTs

This issue is fully discussed in Section II.G.8, *supra*. As noted therein, ComEd has not proposed to alter the existing liability of retail customers for transmission under the OATT.

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Respectfully submitted,

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